BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of San Diego Gas & Electric Company (U-902) for authority to update its gas and electric revenue requirement and base rates effective on January 1, 2008.	Application 06-12-009 (Filed December 8, 2006)
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Order Instituting Investigation on the Commission's own motion into the rates, operations, practices, services and facilities of San Diego Gas & Electric Company and Southern California Gas Company.	Investigation 07-02-013 (Filed February 15, 2007)

REPLY BRIEF
OF THE DIVISION OF RATEPAYER ADVOCATES

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REPLY BRIEF OF THE DIVISION OF RATEPAYER ADVOCATES

1. Introduction/Summary of Recommendations

Pursuant to Rule 13.11 of the Commission's Rules of Practice and Procedure, and the schedule established by Administrative Law Judge (ALJ) Douglas Long, the Division of Ratepayer Advocates (DRA) submits this Reply Brief to address arguments made by some of the parties to the General Rate Case (GRC) Applications of Southern California Gas Company (SCG or SoCalGas) and San Diego Gas and Electric Company (SDG&E) for Test Year (TY) 2008.

Where DRA has already addressed an argument in its Opening Brief, DRA will not repeat it here. Silence on any argument, however, should not be interpreted as agreement or disagreement.

2. Procedural Background

DRA describes the Procedural Background in its Opening Brief at pages 13-15.

3. Policy Issues

3.1 Evidentiary Standards and Burden of Proof

DRA addresses Evidentiary Standards and Burden of Proof in its Opening Brief at pages 15-18.

3.2 Interpretation of the Rate Case Plan

DRA discusses the Interpretation of the Rate Case Plan in its Opening Brief at pages 18-25 and below in this Reply Brief in Section 3.5, "Use of 2006 Recorded Data."

3.3 Base Year 2005 Adjustments

DRA has no comment on this issue as a policy matter, but addresses specific base year 2005 adjustments as they arise in particular areas and below in Section 3.5, "Use of 2006 Recorded Data."

3.4 Adjustment Method To Forecast Test Year 2008

DRA has no comment on this issue as a policy matter, but addresses specific base year 2005 adjustments as they arise in particular areas.

3.5 Use of 2006 Recorded Data

In their Rebuttal testimony, various witnesses for Applicants argued that DRA's use of the 2006 data was somehow barred by the Commission's Rate Case Plan decision. None of Applicants' witnesses ever identified where in the Rate Case Plan this prohibition could be found. In fact, there is no such bar that is even remotely applicable to DRA and the Interveners here.

In the Policy section of their Opening Brief, Applicants seem to have retreated from their previous position and now argue that "[t]he clear intent of the Rate Case Plan is that DRA shall file their testimony 11 weeks after Applicants – which implies the use of the same base year historical data for an application filed in early December 2006."[1] DRA does not agree with the "implication" Applicants have tortured out of the Rate Case Plan schedule. As numerous Commission decisions have held, and continue to hold, most recent recorded data can be used by DRA and Interveners in their forecasts.

In fact, one such Commission decision is the very decision Applicants now cite to bolster their failed argument against the use of 2006 data: the Commission decision establishing a Rate Case Plan for water utilities.[2]

The Water Rate Case Plan includes an Appendix, which is referred to in the portion of the decision Applicants quote. According to that Appendix:

> Up to 45 days after filing, more recent recorded data used in the application may be provided by the utility and used by ORA in its reports. The utility may also use the data in rebuttal testimony. More recent recorded data are utility plant or expense account balances showing actual historical amounts. The more recent recorded data must be used in the same manner and for the same purpose as the data included in the original application. New or additional items or forecasted costs are not updates to recorded data and will not be accepted.[3]

Thus, neither of the Rate Case Plan decisions Applicants cite supports Applicants' position that DRA and the Interveners are barred from using the most recent recorded information. Nor do Applicants have any policy reason to support their arguments.

As TURN states in its Opening Brief, "[t]he overriding purpose of this GRC is to set a reasonable revenue requirement for 2008." Or, as UCAN says, "[r]ate cases are a search for the truth – reasonable forecasts of spending in a future test year, not a search for management wish lists prepared three years in

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1 Sempra Opening Brief, p. 3.

2 Sempra Opening Brief, p. 8.

3 D.04-06-018, Appendix, p. 13.

advance without including information that would impeach them or provide better estimates."[4]

Applicants, however, argue that, "[i]n order to ensure the efficacy of its decision in this and other rate case proceedings, the Commission must be consistent in its use and application of base year historical records that serve as the foundation for test year forecasts."[5] If there is any Commission decision stating this, Applicants have failed to cite it. DRA has found nothing in its research that supports Applicants' suggestion that the base year is etched in stone and must not be updated by anyone else.

In fact, in the recent decision on the SCE TY 2006 GRC, the Commission stated the opposite:

> As discussed in prior Commission decisions, there are a number of acceptable methodologies for forecasting test year costs. In this GRC, parties have used averages and trends of recorded costs, ***the most recent recorded costs***, as well as forecasts based on budgets or incremental budgets over recorded amounts. Depending on circumstances, one method may be more appropriate than others. Under other circumstances, two or more methods may be equally appropriate. [6]

"Consistency," in any case, is a strange argument for Applicants to make in light of their own selective use of whatever forecasting methodology yields the highest revenue requirement. As DRA noted in its Opening Brief, a number of Applicants' witnesses also used 2006 data when they thought it would support their requested increases.[7]

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[4] UCAN Opening Brief, p. 32.

[5] Sempra Opening Brief, p. 9.

[6] Opinion on SCE TY 2006 GRC, (2006) D.06-05-016, p. 10, emphasis added.

[7] *See* DRA Opening Brief, p. 22, footnote 79 for a partial list of Sempra witnesses who argue for the use of 2006 data.

DRA and all Interveners should be allowed to use in their testimony the estimating methodology that they, in their professional judgment, conclude is the best. It is up to the ALJ and the Commissioners to decide what weight to give those proposed methodologies. In DRA's opinion, recorded data is the "gold standard" of estimating methodologies, for the simple reason that no forecasting or estimating is necessary. It is ludicrous for Applicants to suggest that DRA should be prohibited from using this gold standard in its initial testimony.

3.6 Productivity Issues

DRA addresses Productivity Issues in its Opening Brief at pages 25-26 and in Section 27, Post-Test Year Ratemaking.

3.7 Term for Rates Adopted In This Proceeding

DRA addresses this issue in its Opening Brief at pages 502-505.

3.8 Financial Health

DRA has no comment on this issue as a separate policy matter.

3.9 Utility of the Future Projects

DRA's recommendations relating to enabling ratepayers to capture some of the gains of the Utility of the Future initiatives are discussed in Section 27, Post-Test Year Ratemaking, in DRA's Opening Brief.

3.10 Other

As discussed above and in DRA's Opening Brief, Applicants have attempted to make an issue out of the use of 2006 data when there is no legal, policy or other reason to support them, other than their opposition to any forecast that is less than their own. Similarly, with no Commission decision or policy support, Applicants label as "illogical"[8] and "inappropriate"[9] DRA's forecasting methods for such issues as Pensions and Post-Retirement Benefits Other than

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[8] Sempra Opening Brief, p. 293.

[9] Sempra Opening Brief, p. 305.

Pensions (PBOPs), Working Cash, Medical benefits, and various Incentive Compensation Plans made available to only certain of its employees.

DRA's forecasts in each of these areas are consistent with past Commission decisions and policies. Yet, because the Applicants have used this proceeding to seek increases in every conceivable area generally covered in a GRC, and some outside GRCs,[10] DRA and other parties have had to spend vast amounts of time and resources defending long-standing Commission policies against Applicants' vague claims and unsubstantiated arguments. The most egregious examples, from DRA's standpoint, are discussed below.

Pensions

Commission decisions on pensions have relied on the latest available year end return on pension trust assets calculated by the Utility's actuary.[11] DRA's recommendation does just that. Applicants insist, without citing any legal authority to support them, that rather than use the most recent actual returns Applicants' actuaries provided for pension fund assets, the Commission should use information known to be out of date.[12]

In the past, the Commission has stressed its interest in maintaining the funding necessary to protect employees from an insolvent pension fund; at the same time, however, Commission decisions do not require ratepayers to fund more than that.[13] Applicants have given no legal or policy reason to require ratepayers to pay more than the Utilities' own actuary says they need. In light of the facts, Commission precedent and Commission policy, this should be a non-issue.

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[10] See e.g., SCG-3, p. DGT-8. Applicants request to get BCAP approval in this GRC.

[11] *See e.g.,* Re SCE (2006) D.06-05-016, pp. 171-174; Opinion Authorizing Pacific Gas and Electric Company to Recover Contributions to Its Employee Pension Plan (2006) D.06-06-014, pp. 9- 11.

[12] Sempra Opening Brief, p. 292-293.

[13] *See* Re SCE (2006) D.06-05-016, p. 173.

PBOPs

The same is true of Applicants' request for funding for PBOPs.[14] In their Opening Brief, Applicants argue that the Commission should use the Applicants' PBOPs estimate that is based on a study of corporate bond yields dated December 31, 2005. Yet Applicants' own actuary has performed a more recent study showing an estimate for PBOPs costs of nearly $2 million less for SoCalGas, and $1.3 million less for SDG&E.[15] Applicants cite no legal or policy reason for charging ratepayers the higher rates that would result from using the dated forecast. Applicants' position is especially unpersuasive since both Utilities have two-way balancing accounts that protect them against under-collections. In fact, both Utilities' balancing accounts show the Utilities have over-collected for PBOPs expenses. PBOPs, too, should be a non-issue.

Medical Plan Expenses

With regard to Medical Plan expenses, Applicants' recorded expense data shows an average annual inflation rate of about 8%[16]. Even the Utilities agree that, "[b]ased on the latest rate forecasts provided by Towers Perrin, annual increases are projected to gradually decrease from approximately 9.0% to 7.0% over the long-term."[17] In addition, Global Insight, which the Utilities used to forecast various other expense levels for the test year, shows a rate increase for Group Health Insurance of 5.0% for 2007 and 4.3% for 2008.[18] Despite this evidence, Applicants persist in seeking an increase that is based on the largest possible increase in headcount numbers and the highest inflation rates referenced

[14] Sempra Opening Brief, p. 294.

[15] Ex. DRA-27, p. 27-10; Ex. DRA-15, p. 15-10.

[16] 7.99% in 2006 for SCG (Ex. DRA-35, 35-10) and 8.09% for SDG&E (Ex. DRA-14, p. 14-9).

[17] Ex. SDG&E-13-E, p. GJR/JAH-18, lines 1 -4.

[18] Ex. DRA-14, p. 14-11, footnote 23.

by the actuaries.[19] DRA notes that the end result of Applicants' method for SDG&E, for example, would be an increase of 16.70% from 2005 to 2006, and a 17.26% increase from 2006 to 2007 for medical expenses.[20] Applicants' justification for these monumental increases rests on ever shifting forecasts of headcounts, and forecasts that cannot be reconciled with the workpapers that are supposed to support them.[21] Applicants' showing falls so far short of approaching the burden of proof, that this area, too, should be a non-issue.

Working Cash

Working Cash is included in Rate Base to compensate Sempra's investors for the funds advanced by them. DRA disputes Applicants' proposals for Working Cash for a number of reasons, but mentions here the areas of Cash Balances, Accrued Vacation, and Tax Lead-Lag calculations. In light of long-standing Commission policy and practice, these issues should not be in contention at all.

For Cash Balances, the Commission's Standard Practice (SP) U-16, in effect for decades, states that "... in determining the cash requirement, the only amounts which should be considered are the *required* minimum bank deposits that must be maintained..."[22] Since Applicants have included in their working cash requirements, minimum balances not "specified by the bank," these amounts should be removed.

For Accrued Vacation, DRA follows SP-U-16 and prior Commission decisions, and deducts Accrued Vacation from the Applicants' Working Cash requirement.[23] Applicants' argue that "[v]acation accruals are not a source of

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[19] See 17 RT 2128, lines 5-28, Godfrey/DRA.

[20] Ex. DRA-14, p. 14-10.

[21] 17 RT 2128- 2129, Godfrey/DRA.

[22] Ex. DRA-38, p. 38-4 citing CPUC Standard Practice U-16, pp. 3-4, emphasis added.

[23] Ex. DRA-38, p. 38-5; Re SCE (2006) D.06-05-016, 2006 Cal.PUC LEXIS 189 *418

cash to [them] because the overhead rate, including vacation applied to labor expenses, is simply a mechanism for ensuring that GRC operating expense forecasts include exactly 2080 hours per year of labor costs for each employee."[24] This argument does not explain why long-standing policy and precedent should not apply to Applicants and, in any case, is factually incorrect. The companies pay each employee for 2080 hours per year whether they take vacation or not. The expenses for these hours are already embedded within the base year recorded data.

For tax lead-lag calculations, Applicants argue that the Commission should adopt lag day calculations for Federal Income Tax (FIT) and California Corporate Franchise Tax (CCFT) that are a fraction of the FIT and CCFT lag days the Commission has adopted for other energy utilities in the past.[25] Applicants' method is based on "imputed" calculations of their tax payments, a method which will never properly capture the timing of the tax payments Sempra Energy actually makes. Applicants provide no Commission precedent adopting their approach, and DRA has found none.

Applicants' Working Cash proposals are addressed in detail in DRA's testimony and Opening Brief, but it is clear from the long-established policy and precedent that these proposals are wholly without merit. These should be non-issues.

Incentive Compensation Plans and Long Term Incentive Plans

Applicants seek 100% ratepayer funding for both their Incentive Compensation Plans and their Long-Term Incentive Compensation Plans. Applicants' Incentive Compensation Plans (ICPs) apply only to their non-Union employees and, of those, the majority are Management employees.[26] The terms of the ICPs show that these plans reward employees who provide value to

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[24] Sempra Opening Brief, p. 300.

[25] *See* DRA Opening Brief, p. 447, for citations.

[26] Ex. DRA-14, p. 14-32, Ex. DRA-35, p. 35-34.

shareholders, not service to ratepayers. Payouts will not be made if the Sempra Utilities' Net Income is $425 million or less.[27] Payouts are based 40% on Financial Measures, 20% on Operating Measures and 40% on Individual Performance Measures.[28]

Given the fact that the ICPs are primarily incentive plans for Management employees and are designed to reward Corporate financial goals, DRA recommends ratepayer funding be limited to no more than 50% of a three-year average of the targeted levels. DRA's recommendation is consistent with the Commission decision in PG&E's TY 1999 GRC.[29] In that decision, the Commission stated that "...equal sharing of costs is fair and [] provides appropriate incentives to the utility to perform in ways that benefit ratepayers and shareholders alike."[30]

Applicants' Long Term Incentive Plans (LTIPs) are even more exclusive. The LTIPs provide equity grants, primarily for non-qualified stock options or performance based restricted common stock, that are linked to specific financial or shareholder measures.[31] Applicants state that the "LTIP supports long-term performance as measured by total return to shareholders."[32] The LTIPs benefit only what Applicants call "top management talent," or, as Applicants' witness put it, "pretty much" only Applicants' "directors and above."[33]

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[27] Ex. DRA-35-WP, p. 88.

[28] Ex. DRA-35, p. 35-33.

[29] Application of Pacific Gas & Electric Company (TY 1999) (2000) D.00-02-046, mimeo, p. 260.

[30] Application of Pacific Gas & Electric Company (TY 1999) (2000) D.00-02-046, mimeo, p. 260.

[31] *See e.g.,* Ex. DRA-35, p. 35-38

[32] Ex. SCG-11, pp. GJR/JAH 7-8.

[33] *See* 13 RT 1453, Rowland/ SDG&E/SCG.

In support of requiring ratepayers to pay 100% of the costs of both the ICPs and the LTIPs, Applicants argue that these incentives are "critical to attracting, motivating and retaining top management talent..."[34] DRA is not convinced that ratepayers should be charged 100% for the incentive compensation plans to retain this "top management talent." This "top management," which has a duty to generate returns for shareholders and the financial incentive to see that shareholder interests are met, is certainly not devoting 100% of its "talent" exclusively to ratepayer interests.

Sempra's management was less than forthright in providing information relating to its "Utility of the Future" initiatives. When UCAN asked Applicants to provide any reports or documents relating to cost cutting or operations streamlining efforts, Applicants took over two months to provide the information and have been arguing ever since that, although the costs of the Utility of the Future programs should be borne by ratepayers, the benefits are too "hypothetical" to share with them.[35] In addition, the record is replete with instances of inflated forecasts in nearly every area in which the Utilities presented testimony. It seems that no potential rationale for a revenue requirement increase was overlooked.[36] Even as the Utilities' actual 2006 recorded expenses show their estimates are overstated, the Utilities still cling to their forecasts. In prior GRC decisions, the Commission has sometimes required ratepayers to fund 100% of incentive compensation plans, but the record in this case shows circumstances so very different for Applicants' ratepayers, that even a 50% ratepayer contribution may be overly generous. Applicants' request for 100% ratepayer funding of its

[34] Sempra Opening Brief, p. 286, lines 16-19.

[35] *See* Sempra Opening Brief, p. 18, line 27.

[36] *See e.g.,* Ex. DRA-6, page 6-8, SDG&E's request for "data mining software," or page 6-16, SDG&E's request for additional funding for such things as "three new Mr. Ouch information boards."

incentive plans has no support in the record, or in Commission policy or precedent.

As to the LTIP costs, Applicants do not cite any Commission precedent that requires ratepayers to fund stock options. Stock options are provided to executives as an incentive to enhance shareholder value, which is the reason the option is provided in the form of stock. In the past, stock options were not expensed. Merely because the Securities Exchange Commission now requires stock options to be expensed is no justification to saddle ratepayers with these costs. This, too, should be a non-issue.

There is no dispute that the Utilities should receive sufficient revenue requirement to provide safe and reliable service. There should be no dispute that, so long as the revenue requirement provides the Utilities with sufficient funds to pay these costs, then the method that ensures the least cost to ratepayers should be the method the Commission chooses. Yet, in the areas of Working Cash, Pension, PBOPs, Medical Escalation, and Compensation expenses, Applicants forecast expenses in a way that will charge ratepayers more than the Utilities actually need when other methods would ensure that the Company has sufficient funds, but cost ratepayers considerably less.

There are issues where reasonable minds can differ. However, in light of all the evidence in this record, the issues discussed above are not among them.

4. Procurement/Generation

4.1 Electric Generation (Non-Nuclear) SDG&E-Only

In its Opening Brief, SDG&E criticizes DRA's forecast for Electric Generation: "DRA's approach to the 2006 disallowance is flawed because it looks only at actuals, while completely ignoring the reasons for deviations from the forecast. Such an approach leaves SDG&E unable to fund critical capital projects and should thus be rejected."[37] In fact, however, DRA did consider the reasons for deviation in the forecast. Because SDG&E delayed the Palomar Chiller project until 2007, DRA shifted $4.5 million from 2006 to 2007.[38] SDG&E provided no other reasons for deviations.

5. SONGS

DRA recommends no adjustment to SDG&E's SONG proposals.

6. Electric Distribution Operations (SDG&E-Only)

6.1 Electric Distribution O&M

DRA addressed SDG&E's arguments on these accounts in its Opening Brief. However, SDG&E's Opening Brief contains some additional discussion on Tree Trimming (Account 593.1). SDG&E states that its recommendations are consistent with Commission precedent that "ratemaking must assume normal weather."[39] DRA agrees that the Commission should always try to make the best prediction possible with the data it has, including its best assessment concerning weather patterns. Of course, no one can predict the weather, not even SDG&E. The DRA forecast is not based on some abnormality, but on the three most recent years of actual data. On the other hand, SDG&E states, "funding levels should be set to match SDG&E highest expenditures during the last five years."[40] It is not clear why using the highest spending in the last five years is more normal, especially since SDG&E also states, "San Diego has received below average rainfall for 10 of the past 12 years from 1996-2007."[41] Does this mean that the forecast should not consider the last 12 years of data, which are apparently not normal? Using the three most recent years of recorded data is as reasonable a

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[37] Sempra Opening Brief, p. 26.
[38] DRA Opening Brief, p. 27.
[39] Sempra Opening Brief, p. 68.
[40] Id., p. 67
[41] Id.., p. 69.

forecast as possible for this account, and SDG&E cannot show that its forecast is any more "normal" than DRA's.

SDG&E predicts, "it is highly likely that with the return to normal rainfall, the number of trees require[ing] trimming will increase to levels experienced in 2004."[42] However, SDG&E's data shows that the historical pattern is a long-term decrease in rainfall. A document attached to SDG&E's rebuttal testimony, titled "Water Management: Annual Rainfall amounts at Lindberg Field, San Diego County" shows a decrease in the "Normal Rainfall" from 10.41 inches in 1964 to 10.29 inches in 2005.[43]

SDG&E also provides no justification for switching from a one-way to a two-way balancing account for tree-trimming expenses. The requested two-way balancing account eliminates all cost-reducing incentives. It is a blank check. As SDG&E states, "there is no annual limit."[44] Furthermore, it is an unwarranted change in Commission policy that shifts risks to the ratepayers.

6.2 Electric Distribution Operations-Capital Expenditures

DRA addressed SDG&E's arguments on Electric Distribution Capital Expenditures in its Opening Brief. However, a few additional points in response to the Sempra Opening Brief are discussed below.

6.2.1 Use of 2006 Recorded Data for SDG&E's Capital Expenditures

Firstly, SDG&E alleges in its Opening Brief that DRA inappropriately changed the base year to 2006 when it used recorded 2006 data in preparing its comparison graph of recorded/forecast data.[45] As discussed in Exhibit DRA-7, Graph 7-1 was not used for trending purposes; it was only a tool used to judge

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[42] Id., p. 70.

[43] Ex. SDG&E-211 A, the document is contained in the 3rd to last and 2nd to last pages.

[44] Sempra Opening Brief, p. 116.

[45] Sempra Opening Brief, p. 82. The graph is in DRA-7, p. 7-6.

how SDG&E's forecasted expenditures compared to recorded data.[46] Apparently, SDG&E contends that DRA should be prohibited from doing that type of fundamental comparison. SDG&E then states that DRA used an "exaggerated scale" (along with using 2006 data) to create a downward graph. SDG&E's basic math is wrong. The scale that was used has nothing to do with whether the trend was positive (trending up) or negative (trending down). The downward slope is completely determined by the data points chosen-in this case the inclusion of recorded 2006 data by DRA, while SDG&E used estimated 2006 data. The scale that DRA used was simply chosen so that it would fit on the bottom of p. 7-6 of DRA-7. If DRA had chosen the vertical scale that was used by SDG&E[47] the downward trend would have been more pronounced. If anything, the scales chosen by DRA minimized the slope of the downward trend of the graph.

Additionally, in its Opening Brief SDG&E changed the forecasted data points in its version of the comparison graph. SDG&E's brief displays copies of both DRA's original comparison graph and SDG&E's version of the graph.[48] SDG&E provided copies of both DRA's original comparison graph and SDG&E's version of the graph on page 83 of Sempra's Opening Brief. DRA's graph (the upper one on page 83 of Sempra's brief) ties to Table 7-1 on page 7-3 of Exhibit DRA-7. Using 2007 as an example, DRA's graph shows an SDG&E forecasted amount of slightly over $200 million, with DRA's forecast being slightly less than $180 million. This ties to line 21 of Table 7-1, which shows $201.325 million and $177.633 million for SDG&E and DRA in 2007. However, the corresponding numbers in SDG&E's version of the comparison graph (the lower one on page 83) are considerably different. Again using 2007 as an example, SDG&E's forecasted amount is shown as slightly over $190 million, with DRA's forecast being in the

[46] Ex. DRA-7, p. 7-7, line 17.

[47] Sempra Opening Brief, p.83, Figure CAW-1.

[48] Id., p. 83.

high $180 millions. Clearly, SDG&E has changed the forecasted data that it has included in its version of the graph. It is misleading and erroneous for SDG&E to give its version of the comparison graph the heading "Data from DRA Graph 7-1 Shown with Normal Scaling." Not only is the scaling not "normal" (as has been discussed previously), but it is not even DRA's data!

6.2.2 Expenditures for Indirect Capitalized Overheads Related to Project 213

DRA addresses this issue in its Opening Brief at pages 53-55.

6.2.3 Project 99299-Future Capacity Projects

SDG&E criticizes DRA's adjustments to Project 99299, calling DRA's analysis that capital forecasts for unexpected capital additions should not be included when there is no similar expenditure reduction for unexpected cancellations or delays a "complete red herring."[49] SDG&E states that capital projects are not allowed into rate base until they are used and useful.[50] While certainly true, DRA is puzzled as to what this has to do with DRA's argument that there is no mechanism to reflect the fact that forecasted projects are often reduced/cancelled/delayed. As SDG&E certainly knows, all forecasted capital projects that are proposed in the GRC (and adopted by the Commission) will be entered into rate base upon their completion dates. At that time they begin earning a return, and will continue to do so during the entire rate case cycle. At the time of the <u>next</u> GRC, the proposed capital expenditures for this <u>current</u> GRC are "trued-up" by using recorded rate base data in the base year. However, until that true-up occurs, SDG&E will earn a return on all of its proposed capital expenditures at the time they are completed, unless adjusted by DRA or other interveners. Is SDG&E suggesting that the forecasted capital expenditures in this GRC do not get included in rate base in the RO model? This is untrue – forecasted capital expenditures,

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[49] Sempra Opening Brief, p.84.
[50] Id.

unless modified by DRA or other Interveners, do get added to rate base in the RO model. DRA's argument regarding reduced/cancelled/delayed capital projects continues to be valid.

SDG&E's Table CAW-1 purports to show that since the GRC was filed, an additional $5.956 million in capital expenditures were added for 2007, and an additional $4.322 million were added for 2008.[51] Evidently, the purpose of this table is to show that the expenditures on new additions for 2007 and 2008 already exceed the amounts ($2.993 million) provided for in Project 99299. As discussed at length in DRA's Opening Brief (pages 56 and 57), Table CAW-1 is meaningless because it does not address the capital projects that will be reduced/cancelled/delayed. SDG&E cannot deny that such reductions/cancellations/delays routinely occur; in its Opening Brief, DRA pointed out that SDG&E itself has already identified four projects, totaling over $15 million, that are being delayed past the 2008 test year.[52] In DRA's experience, it is inevitable that other unidentified capital projects will also be reduced/cancelled/delayed. DRA's proposed adjustment is very simple and very fundamental. Put simply, SDG&E should not be allowed to reflect unidentified capital additions unless it also reflects unidentified capital reductions/cancellations/delays; since it has not done the latter, it should not be allowed to do the former.

6.2.4 Expenditures For Reliability/Improvement Projects Based on Project 99282 Expenditures

In its Opening Brief, SDG&E raises several arguments in an effort to counter DRA's position that SDG&E's forecasts for this account are too high. SDG&E first claims that DRA's analysis of this adjustment simply consists of stating that "a doubling of average historical expenditures is a large increase" and

[51] Sempra Opening Brief, p. 85.
[52] DRA Opening Brief, p. 57.

then claiming that this is reasonable.[53] However, as discussed in DRA's Opening Brief, SDG&E's allegation completely ignores the fact that DRA carefully examined the historical expenditures and factored in the other capital projects (projects that DRA has allowed) that are specifically designed to reduce obsolete equipment.[54]

SDG&E further alleges that underfunding of Project 99282 will degrade system reliability, and that it is necessary to replace aging and obsolete equipment before customer service suffers. It then discusses how the failure of a 4kV circuit breaker caused an outage, and that there are 26 more of the same vintage 4kV breakers remaining on the SDG&E system.[55] DRA agrees that it is important to prevent the degradation of SDG&E's electric distribution system; it is especially important to prevent customer service problems. As mentioned previously, DRA recommends that expenditures for this project be doubled over historic levels, that other capital projects that address reliability/improvement issues be undertaken,[56] and that Aging Infrastructure expenditures (which SDG&E has budgeted at $69 million) be carried out. DRA is convinced that its recommendations protect both the distribution system and the reliable service that SDG&E's customers currently enjoy. One example of how SDG&E seems to be ignoring these protections is the 4kV circuit breaker issue. SDG&E mentions these old circuit breakers as an example of how its distribution system needs to be maintained and obsolete equipment needs to be replaced. However, this example also illustrates DRA's contention that other capital projects (separate from Project 99282) are helping to replace obsolete equipment, and that these other projects should not be ignored when forecasting reasonable expenditure level for Project 99282. Project 06260, a

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[53] Sempra Opening Brief, p. 85.

[54] DRA Opening Brief, p.59

[55] SDG&E Opening Brief, p.86.

[56] Ex. DRA-7, page 7-16, lines 8 through 18.

capital project that DRA has found reasonable, specifically earmarks 4kV substations for replacement. This clearly shows that the pool of obsolete substation equipment will be reduced by projects other that 99282.

SDG&E also mentions that its proposed funding levels will address the problem of aging equipment within 4 years, while it would take 7 years using DRA's recommended levels.[57] SDG&E does not mention whether those time frames take into consideration the impact that other related capital projects and Aging Infrastructure expenditures will have on replacing obsolete equipment; if they do not, then those time frames will be much shorter. However, even if these other projects are factored in to these intervals, that does not indicate that DRA is being imprudent when it recommends adding an additional three years to the replacement schedule. As discussed in more detail in DRA's Opening Brief[58], SDG&E is vigorously addressing reliability issues in a number of different projects, and is making steady improvements to its distribution system. Its customers believe that SDG&E does a good job of preventing outages, and do not favor additional expenditures in this area. Combining all these facts with DRA's recommendation that Project 99282 expenditures be doubled, it is clear that the reliability of SDG&E's electric distribution system will be maintained (if not substantially improved) with DRA's recommended expenditure levels.

6.2.5. Expenditures for Reliability/ Improvement Projects Based on Project 99282 Expenditures

DRA addresses this issue in its Opening Brief at pages 57-60.

[57] SDG&E Opening Brief, p. 6.

[58] DRA Opening Brief, pp. 59-60

6.2.6 Expenditures For Reliability/Improvements Projects Based on Project 230

In its Opening Brief, SDG&E presents a number of arguments that purport to show how DRA's recommendations are flawed.[59] SDG&E discusses: how branch (also known as lateral) cable failures are increasing (and includes Chart CAW-2 to illustrate this); how the PG&E/KEMA cable replacement schedule is allegedly not applicable to SDG&E; how DRA has not taken into consideration the fact that all existing cables (not just the unjacketed cables that are prone to failures) are aging; how the replacement schedule that results from DRA's recommendations are allegedly too long; how other DRA witnesses have allegedly recommended that additional aging infrastructure should be added; and how SDG&E's customers want reliable service. With one exception, DRA anticipated these arguments, and has discussed them at length in its Opening Brief, beginning on page 62. DRA urges that its Opening Brief be reviewed to understand the flaws in SDG&E's arguments.

The one exception that was not previously discussed by DRA was SDG&E's contention that DRA has ignored "the fact that all existing cables (both the high failure rate unjacketed cables and all other cables) continue to age every day."[60] This is certainly a true statement, but as far as DRA can tell, it has nothing to do with DRA's analysis. In Exhibit SDG&E-4, page CAW-256, lines 11 and 12, SDG&E describes the purpose of Project 230:

> *This project will provide for the replacement of the portion of remaining unjacketed cable that has high failure rate. (Emphasis added.)*

The description then goes on to list the remaining miles of unjacketed cable in SDG&E's system. DRA did not find this description unusual; what would have been unusual would be SDG&E devoting cable replacement dollars to the recently

[59] Sempra Opening Brief, pp. 87-89.

[60] Sempra Opening Brief, p. 88.

installed <u>jacketed</u> cables, which are more reliable than the older <u>unjacketed</u> cables. Based on SDG&E's description of Project 230, as well as DRA's knowledge that the more recently installed jacketed cables are both newer and more reliable, it is reasonable to assume that the vast majority of dollars forecasted to be expended for Project 230 will be spent on replacing unjacketed cables. When SDG&E states that DRA's analysis "doesn't take into account that the remaining 7,251 miles of cable is constantly aging"[61], SDG&E is ignoring the obvious fact that, because it is newer and more reliable, there is no immediate need to factor in the newer cable. SDG&E appears to acknowledge this when it states "<u>in time</u>, some of the remaining 7,251 miles of cable will also continue to fail…."[62]

6.2.7 Expenditures for IT Projects

In its Opening Brief, SDG&E does not discuss this adjustment to any great extent. It does mention that the IT costs were found in the exhibits/workpapers of SDG&E's IT witness J. Chris Baker, not in the Electric Distribution material.[63] This is true, but it is irrelevant to DRA's analysis. Since the description/discussion/justification for these specific IT projects were contained in the Electric Distribution exhibits/workpapers, that is where DRA has elected to reflect the adjustments. Where the adjustments for these specific IT capital projects are reflected makes no difference, as long as the adjustments are not reflected more than once. As was mentioned in Exhibit DRA-7, DRA took care to ensure that no duplication of these adjustments occurred.[64]

SDG&E also states that it continually manages a portfolio of IT projects.[65] Again, this may be true, but DRA does not understand how this negates the fact

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[61] Sempra Opening Brief, p. 89.

[62] Sempra Opening Brief, p. 88, emphasis added.

[63] Sempra Opening Brief, p. 89.

[64] Exhibit DRA-7, pp. 7-6, lines 3 through 5.

[65] Sempra Opening Brief, p. 89.

that SDG&E itself is admitting that it is deferring IT projects to periods beyond the test year. It appears that SDG&E is asking the Commission to give it a "blank check" that it can use as it pleases. As discussed in DRA's Opening Brief on page 66, SDG&E has not provided DRA with a list of which projects it now proposes to add, the costs of those projects, or the justifications for them. Regulation does not work that way. SDG&E has the burden to provide the Commission with sufficient details and justifications so as to enable the Commission to determine that the projects are reasonable. Obviously, since SDG&E has not provided DRA with any details regarding these "replacement" IT projects, it has completely failed to meet its burden. DRA's recommended IT capital disallowance should be adopted.

6.2.8 SDG&E's Report on Land Acquisitions

DRA addresses this issue in its Opening Brief at page 67.

6.2.9 Reduction to RO Model to Reflect 2006 Actual Expenditures in Other DRA Exhibits

DRA addresses this issue in Section 26 of the Reply Brief, which is where SDG&E addressed it in Applicants' Opening Brief.

7. Gas Distribution Operations

7.1 Common Issues

7.1.1 Integrity Management Programs for Distribution Pipelines

In its Opening Brief, DRA has already addressed the arguments the Utilities make for ratepayer funding of approximately $36.8 million for various O&M expenses and capital expenditures associated with the Distribution Pipeline Integrity Management regulations.[66] These regulations are expected, but have not yet been adopted by the Department of Transportation (DOT). Consequently, Applicants' requested increases are both premature and speculative. DRA, therefore, recommends that, after the DOT issues the final rules for this program,

[66] DRA Opening Brief, p. 70.

SCG and SDG&E be authorized to file an advice letter to establish a memorandum account for these costs. The memorandum account will allow the Utilities to record certain authorized costs for future recovery through rates.

In its Opening Brief, the Southern California Generation Coalition (SCGC) points out that, "not only is it unclear as to when these gas pipeline integrity management requirements might be imposed on the distribution system but *it is also unclear as to exactly what SoCalGas will be required to do and how rapidly SoCalGas will be required to complete the work*."[67] DRA agrees.

For example, it appears that the DOT regulations for Transmission lines, which Applicants offer as a comparison,[68] were phased in over years. As the Applicants state, "[a]lthough the law requiring TIMP was passed in December 2002, the program continues to evolve today with a significant degree of uncertainty concerning the cost of assessments, especially the non-piggable more numerous, and relatively shorter length pipeline segments which will increasingly dominate the schedule through 2012."[69] Assuming that the Distribution Pipeline regulations follow that pattern, there is no justification to include these speculative estimates in base rates. Finally, Applicants' reference to the DOT's *Integrity Management for Gas Distribution Pipelines* report[70], offers no more information as to what requirements will be imposed and when, reinforcing DRA's recommendation that these costs should be the subject of a memorandum account.

SCGC also proposes that the memorandum account be interest-bearing and "subject to review for reasonableness during the next SoCalGas general rate case."[71] SCGC notes that [s]everal of SoCalGas' recently created memorandum

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[67] SCGC Opening Brief, p. 8, emphasis added.
[68] Ex. SDG&E-215, p. 3.
[69] Ex. SCG-214, pp. 21-22.
[70] Sempra Opening Brief, p. 143.
[71] SCGC Opening Brief, p. 8.

accounts allow recovery through the annual update process. As a result, the memorandum accounts function more like balancing accounts than memorandum accounts."[72] DRA supports SCGC's proposal that the final Commission decision include a directive that the balances in the account shall be subject to reasonableness review in the next GRC.

7.2 SoCalGas Issues

DRA's Opening Brief addresses these issues at pages 73-113.

7.2.1 Gas Distribution O&M expenses

DRA addresses SCG Gas Distribution O&M expenses at pages 74-104 of its Opening Brief.

7.2.2 Capital Expenditures

For Gas Distribution Capital Expenditures, DRA has consistently included recorded 2006 data in its forecasts. SCG, on the other hand, has selectively chosen to use 2006 data in order to increase its forecasts. However, SCG has not made any adjustments to its original forecasts for 2007 and 2008. As a result of its upward adjustments to 2006 data, SCG has increased its 2006 forecast from $179.2 million to $183.9 million.[73] While DRA supports using of the most recent data for forecasts, SCG's technique of accepting portions of DRA's forecasts that grant the company a higher forecast (use of 2006 actual data) while ignoring the accompanying analysis on 2007 and 2008 forecasts is not supportable by the evidence. SCG's use of 2006 data without consideration of the impacts on other years' spending is unpersuasive. SCG forecasted its 2006-2008 data based on cost and spending assumptions which have since changed. This is evident from the large difference between forecast and actual for many of these accounts. DRA's analysis attempted to capture the fact that, because spending was different than

[72] SCGC Opening Brief, p. 9.

[73] Sempra Opening Brief, p. 116.

anticipated in 2006, some adjustment should be made to the 2007 and 2008 data to account for shifting in budgets and priorities.

For "uncontested" accounts where DRA recommends use of 2006 actual data, but has made no other analysis or adjustments, SCG has readily agreed to this actual data in order to increase its forecasts.[74] For accounts where DRA has adjusted SCG's 2007 and 2008 forecasts, SCG disagrees with DRA. For accounts such as New Business, DRA has no idea why SCG opposes its recommendations since the three years of capital forecasts for both DRA and SCG result in the same total.[75] Certainly, SCG does not have a problem with using 2006 data since it has accepted it for all the "uncontested" capital groupings. SCG states, "DRA's recommendation, at a minimum for years 2007 and 2008, must be rejected in favor of SCG's forecast… ."[76] Possibly, SCG hopes that the Commission will adopt DRA's forecast for 2006 ($54.433 million versus SCG's $35.7 million), while also accepting SCG's forecasts for 2007 and 2008, which are higher than DRA's. The same analysis applies to Pressure Betterment and Field Capital Support, where DRA's three-year forecast equals SCG's.[77] SCG apparently does not object to using the higher 2006 number, but opposes any adjustments to 2007 and 2008. This, too, is unreasonable. If DRA or the Commission accepted the higher than forecast 2006 actuals for all accounts, and did not make any offsetting adjustments in 2007 and 2008 as DRA did for many accounts, then this would result in a higher recommendation than what SCG asked for in its application.

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[74] Sempra Opening Brief, p. 16.

[75] DRA Opening Brief, p.109.

[76] Sempra Opening Brief, p. 118.

[77] DRA Opening Brief, pp. 10-113; Sempra Opening Brief, pp. 118-121.

7.3 SDG&E Issues

7.3.1 Summary of Recommendations

DRA summarizes its recommendations in its Opening Brief at pages 113-114.

7.3.2 Discussion/ Analysis of O&M Expenses

DRA's recommendations for this area are discussed in DRA's Opening Brief at pages 114- 116.

7.3.3 Capital Expenditures

For Capital Expenditures, SDG&E's approach to selectively use 2006 data where it increases its forecasts, but not where it decreases the forecast should not be adopted. As a result of SDG&E's update for certain 2006 data, SDG&E's 2006 Gas Distribution Capital forecast increased from $15,977,000 in its testimony to $16,902,000.[78] SDG&E states that "use of the adjusted recorded data may result in biasing *any* forecast result."[79] Three pages later, the company accepts DRA's forecasts in accounts where the 2006 recorded is higher than forecast (budget codes 500, 506 and 508), but not where the 2006 recorded is lower (budget codes 502, 503 and 505).[80] SDG&E also adopts 2006 actual spending for "uncontested" areas where the actual data was higher than forecast.[81] For these accounts, SDG&E provided no additional analysis or rationale on why such use of 2006 data did not result in the biases of which it warned.

In accounts where SDG&E disagreed with DRA's forecasts, a reccurring theme is that the SDG&E forecast was developed through "specific identified projects."[82] Just because SDG&E forecast certain spending in its testimony does

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[78] Sempra Opening Brief, pp. 131-132.
[79] Sempra Opening Brief, p. 128, emphasis added.
[80] Sempra Opening Brief, p. 131.
[81] Sempra Opening Brief, p. 123; Ex. SDG&E/SCG-300, p. E-4.
[82] Id., p. 133.

not mean that it will proceed with all of these projects when 2007 and 2008 roll around. Capital projects are often delayed or deferred. For instance, it is possible that the anticipated load growth mentioned in the Account 503 discussion[83] will not materialize. This issue is also discussed in Section 6.2 of this reply brief.

8. Gas Transmission

8.1 Common Issues

In its Opening Brief, DRA addresses Gas Transmission issues separately by Utility.

8.2 SoCalGas Issues

In its Opening Brief, DRA addresses SoCalGas Transmission issues at pages 120-127.

8.3 SDG&E Issues

In its Opening Brief, DRA addresses SDG&E transmission issues at pages 134-142.

9. Gas Storage and Engineering

9.1 Gas Storage (SoCalGas-Only)

In its Opening Brief, DRA addresses Gas Storage (SoCal Gas Only) issues, including the proposed settlement between SoCalGas and Local 483, at pages 142-147.

9.2 Gas Engineering

9.2.1 Common Issues

In its Opening Brief, DRA addresses Gas Engineering issues separately by Utility.

[83] Sempra Opening brief, pp. 132-133.

9.3 SoCalGas Issues

In its Opening Brief, DRA addresses SoCalGas Engineering issues at pages 147-153.

9.4 SDG&E Issues

In its Opening Brief, DRA addresses SDG&E Engineering issues at pages 153-157.

10. Customer Service

10.1 Operations - Common Issues

In their Opening Brief, the Sempra utilities are highly critical of DRA's analysis of Customer Service Operations costs. According to Sempra, DRA's testimony consists of a "fatally flawed use of arbitrary forecasting methods"[84] and, "in a shameless attempt to 'cherry pick' disallowances, DRA employs zero consistency in its selection of historical data upon which to base its forecasts."[85] DRA did employ a number of forecasting techniques in its analysis of the Customer Service Operations. This is because, rather than performing a simple "top down" analysis of historical averages, the DRA witness actually considered each and every cost driver the company discussed for each account, sub account and "activity." This approach, while extremely labor intensive, allowed the witness to fairly test the reasonableness of the companies' forecasts. For instance, as shown on p. 164 of DRA's Opening Brief, DRA had to perform a number of adjustments in various cost categories just to obtain a customer services field order volume, which, in turn, was used to generate an account 879 forecast. To label DRA's detail-oriented approach to forecasting these cost categories as arbitrary cherry picking is absurd, especially when reviewing these accounts through a "top

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[84] Sempra Opening brief, p.150.
[85] Id., p.151.

down" approach. Shown below are the historical figures for Customer Service Operations accounts and the DRA and Sempra recommendations.

SCG Customer Services Operations
Recorded Adjusted O&M Expenses[86]
(In Thousands of 2005 Dollars)

FERC Account	Recorded Adjusted 2003	Recorded Adjusted 2004	Recorded Adjusted 2005	Recorded Adjusted 2006	SCG Forecast 2008	DRA Forecast 2008
879	**$87,806**	**$89,981**	**$88,260**	**$90,476**	**$100,982**	**$94,399**
903	**$87,276**	**$84,058**	**$85,440**	**$86,197**	**$88,624**	**$87,416**
Total of all Accounts	$219,397	$216,747	$220,401	$223,156	$239,144	$231,353

SDG&E Customer Service Operations
Adjusted Recorded O&M Expenses[87]
(In Thousands of 2005 Dollars)

FERC Account	Adjusted Recorded 2003	Adjusted Recorded 2004	Adjusted Recorded 2005	Adjusted Recorded 2006	SDG&E Forecast 2008	DRA Forecast 2008
586	$6,421	$6,948	$6,934	$8,232	$8,898	$7,937
878	$3,134	$3,653	$3,285	$3,047	$4,358	$3,289
879	$8,011	$7,442	$7,380	$7,998	$9,489	$8,037
902	$9,311	$9,707	$9,480	$9,827	$10,448	$10,021
903	$29,657	$28,745	$28,026	$28,292	$30,876	$30,183
Total of All Accounts	$56,534	$56,495	$55,105	$57,396	$64,069	$59,944

As shown above, DRA's forecast is higher than all recorded years in almost every instance. Sempra's accusations of cherry-picking do not stand up, because if DRA had used any singular forecasting methodology for any of these accounts, the forecast would have been lower than DRA's forecast. For the SCG accounts,

[86] Ex. DRA-32, p.32-4.

[87] Ex. DRA-11, p. 11-3.

DRA's forecast is higher than every recorded year except 2006 (whose use Sempra objects to for these accounts) for account 879. Would SCG really have preferred that DRA used a "consistent" two-year, three-year or four-year average? For SDG&E, DRA's forecast is also higher than any multi year average forecast technique. For Accounts 586 and 878, DRA's forecast is only lower than 2006 and 2004, respectively, and is higher for all other years for all the other accounts shown above. Yet, Sempra maintains that DRA cherry-picked. DRA's goal, and its responsibility in this case, is to come up with the best, most reasonable forecast for the Commission's use. Consistency in forecasting technique, both within a business unit and company wide, is not always the most reasonable forecast.

Interestingly, another SDG&E witness acknowledges this point in testimony, and it is repeated in Sempra's Opening Brief:

> Averaging of recorded costs, trends of recorded costs, the most recent recorded costs, and incremental budgets over recorded costs are different approaches that might produce the most reasonable forecast for an account.[88]

DRA agrees with this sentiment, but apparently it is not shared by all factions of the Sempra utilities.

Generally, SCG's arguments are the same as those made in its rebuttal testimony and were anticipated by DRA in writing its Opening Brief. However, SCG did make one incorrect citation to the transcript. SCG states, "DRA Witness Ms. Chia, on the other hand, acknowledges that if the need for gas quality monitoring arises during the attrition period, provision of that service by SDG&E is prudent and critically important. (Transcript, pp. 2177-2178.)"[89] However, a review of the transcript shows that Ms. Chia never said this:

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[88] Sempra Opening Brief, p. 36.

[89] Id., p. 154.

> Q It's my understanding that you are recommending no funding for gas-quality monitoring because you believe there will be no need for it in 2008. That's correct.
>
> A Correct.
>
> Q And I am asking you if the need arose subsequent to that, let's say within the attrition period, 2009, 2010, would you change your opinion that the funding is needed?
>
> A That's kind of hard to say because I really don't know. I haven't seen anything to show me that.[90]

DRA continues to recommend that its forecasts be adopted.

11. Emergency Preparedness

DRA addresses these issues separately by Utility in DRA's Opening Brief at pages 227- 231.

12. Information Technology

12.1 Common Issues

In their Opening Brief, Applicants repeat the arguments they made in their Rebuttal testimony relating to Information Technology (IT). DRA has already addressed those arguments in its Opening Brief.[91] Below, DRA addresses only three recurring factual errors.

In their Opening Brief, Applicants state that "DRA ... utilized a trending approach to forecast 2008 O&M costs based on 2005 and 2006 actual expenses and customer growth rates specific to each utility ranging from 1.17% to 1.52%."[92] Applicants are only partially correct. DRA based its forecast on the 2006 recorded expense data Applicants provided increased by customer growth.[93]

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[90] DRA/Chia, 17 RT 2178

[91] DRA Opening Brief, pp. 231- 240.

[92] Sempra Opening Brief, p. 188-189.

[93] Ex. DRA-17, p. 17-6.

DRA did ***not*** use 2005 data to develop its forecast for O&M expenses. DRA used 2005 data only as a reference to verify that its forecast was consistent with Utilities' spending in the recent past.[94] Consequently, Applicants' arguments about trending, and adjustments to 2005 are largely irrelevant to DRA's actual recommendations.

DRA continues to recommend that the Commission adopt DRA's O&M proposals so that ratepayers are not paying expenses for projects that have not been approved, or were postponed or canceled.

As to IT Capital expenditures, Applicants continue to make two arguments that DRA would have expected to be withdrawn by now since neither is accurate. First, Applicants state that DRA's proposal to only allow costs for projects with completed business cases is "inconsistent with SDG&E/SCG's internal procedures utilized for many years." The only citation Applicants give for this statement is the exact same statement that appeared, also unsupported, in Applicants' Rebuttal testimony.[95]

DRA's recommendations, on the other hand, are based on the procedures set forth in the Applicants' own IT product manual which Applicants' witness testified is "actually in continued use."[96] According to the IT manual, projects start at the "concept" phase, and then proceed to the "business case" phase. From the IT manual, it is clear that only in the business case phase is the "concept" defined to "the level of detail necessary to establish a fixed price and fixed timeline proposal for the subsequent phase(s) of the project, including build vs. buy and reusable components analysis and decisions."[97] It is also at the "business case phase" that projects go through the process "to review consistency to internal

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[94] Ex. DRA-17, p. 17-7.

[95] Ex. SDG&E/SCG-232, p. 6, line14.

[96] 12 RT 1226, JCBaker/ SCG/SDG&E.

[97] Ex. DRA-58, p. 13.

information technology standards and architectures," and "validate proposed business benefits."[98]

For projects without an approved business case, then, it is clear from Sempra's own IT manual that there is no factual basis to conclude that the there will be any business benefits, or "that the project will not adversely impact the existing or planned IT infrastructure or enterprise solution," or that it will "adhere to existing or planned information technology system and component performance standards."[99] Thus, contrary to Applicants' Opening Brief, Sempra's "internal procedures utilized for many years" show that it would be unreasonable to require ratepayers to fund projects without a management-approved business case.

Finally, Applicants argue that DRA's proposal is "inconsistent" with procedures "included in the most recently Commission approved Cost of Service ..." The most "recently Commission approved Cost of Service decision" adopted a settlement. Pursuant to Rule 12.5 of the Commission's Rules of Practice and Procedure, "[u]nless the Commission expressly provides otherwise, .. adoption [of a settlement] does not constitute approval of or precedent regarding any principle or issue in the proceeding, or in any future proceeding.[100]

DRA continues to recommend that the Commission adopt DRA's IT proposals.

[98] 12 RT 1229 JCBaker/ SDG&E/SCG.

[99] See Ex. SCG-12, p. JCB-8.

[100] Rule 12.5 Adoption [of Settlement] Binding, Not Precedential.

13. Business Solutions/Support Services

13.1 Common Issues

13.1.1 Proposal of the California Natural Gas Vehicle Coalition

DRA has already addressed in its Opening Brief the arguments the California Natural Gas Vehicle Coalition (CNGVC) made in its testimony.[101] Below, DRA addresses two new arguments CNGVC made in its Opening Brief.

CGNVE mentions testimony filed by the Sempra Utilities in another Commission proceeding, the Application of SDG&E and SoCalGas for Approval of Proposals Set Forth in their Joint Climate Action Initiative (CAI), A.07-08-031. To DRA's knowledge, none of that testimony is in the record in this GRC proceeding.

While DRA agrees that the Commission should take care to ensure that the Utilities do not receive duplicate funding for low emission vehicles, DRA's opposition to the rate increase proposal of CNGVC in this proceeding remains unchanged. As described in DRA's Opening Brief, these proposals are both barred by Commission policy and are not supported by the record.

In its Opening Brief, CNGVC says that its request for additional funds for "customer education and information," originally described by CNGVC in Opening Testimony as "lobbying," is actually not "*lobbying*," it is "*advocacy*."[102] Whatever label the CNGVC now chooses for its proposed activities, the descriptions CNGVC itself provided in its testimony still fall within the "long-standing Commission policy prohibit[ing] rate recovery of any costs for political lobbying or advocacy."[103]

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[101] DRA Opening Brief, pp. 240-245.

[102] *See* CNGVC Opening Brief, p. 5.

[103] Opinion Authorizing Pacific Gas & Electric Company's GRC Revenue Requirement for 2007 – 2010 (2007) D.07-03-044, p. 153.

In testimony, CGNVC stated that additional funding should be used by the Sempra Utilities to "work cooperatively with appropriate industry advocacy groups, air quality organizations (e.g. CARB, the South Coast Air Quality Management District[SCAQMD], Air Pollution Control Districts), prominent California public officials...," to "...advocate the use of natural gas vehicles with municipal and county governments....," and to "....educate public officials about the ... economic, health and air quality benefits of CNG and LNG fueled vehicles, including the availability of financial incentives."[104]

By CNGVC's own words, the activities for which it seeks increased ratepayer funding are all within the definition of lobbying activities that the Commission has repeatedly disallowed in the past. In fact, in a decision relating to requests by energy utilities for ratepayer funding of low emission vehicle programs, the Commission noted that the utilities had not demonstrated that certain costs would be used for purposes "other than to influence legislation or rulemaking."[105] The same is true here.

Whatever term CNGVC uses to characterize its plans, the record shows no reason, other than the implicit financial interest of some of CNGVC's members,[106] why ratepayers should be required to help this special interest group promote the purchase of NGVs as opposed to some other low-emission vehicles. In fact, the Commission has already considered this issue and found, that "[iI]t is not reasonable for SoCalGas to spend any ratepayer funds on activities that promote the purchase of natural gas vehicles instead of the purchase of vehicles using another type of fuel."[107] As the Commission found in connection with an

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[104] Ex. CNGV-1, pp. 15-16.

[105] Re Utility Involvement in the Market for Low-emission Vehicles (1995) 62 CPUC 2d 395, 424 – 426, D.95-11-035.

[106] Ex. DRA-68. The CGNVC members include natural gas suppliers and natural gas vehicle manufacturers.

[107] Re Utility Involvement in the Market for Low-emission Vehicles (1995) 62 CPUC 2d

SCE proposal to have ratepayers fund "technology introduction and customer education," for electric vehicles, "[v]ehicle and battery manufacturers should bear the burden of displaying and advertising their products."[108] The same is true for the CNGVC.

DRA continues to recommend $0 ratepayer funding for the CGNVC proposals.

13.2 SoCalGas Issues

DRA addresses these issues in its Opening Brief at pages 245-254.

13.3 SDG&E Issues

DRA addresses these issues in its Opening Brief at pages 255-261.

14. Administrative and General – Non-Shared Services

14.1 Common Issues

In their Opening Briefs, Applicants repeat the arguments they made in their Rebuttal relating to Administrative and General (A&G) Non-Shared Services. DRA has already addressed those arguments in its Opening Brief.[109] Nothing in Applicants' Opening Brief causes DRA to change its recommendations. Below DRA addresses one argument SDG&E makes in connection with its requested increase for accounting operations to underscore the inadequacy of Applicants' showing.

14.2 SoCalGas Issues

DRA addresses these issues in its Opening Brief at pages 257-276.

395, 447.

[108] Re Utility Involvement in the Market for Low-emission Vehicles (1995) 62 CPUC 2d 395, 424.

[109] DRA Opening Brief, pp. 262-286.

14.3 SDG&E Issues

14.3.1 FERC Account 920.0 – Non-Shared Services A&G Labor – Accounting Operations Labor

In its Opening Brief, SDG&E argues that it has justified its requested increase for accounting operations because "[g]rowth in new capital expenditures at SDG&E is on the rise, with $1.5 billion to $1.7 billion per year in total capital expenditures forecasted in the coming years."[110] According to Applicants, "SDG&E's total capital expenditures are forecasted to triple in 2008 compared to 2005 and Cost Accounting will need to support all these activities."[111]

As DRA noted in its Opening Brief, Applicants did not mention these "new capital expenditures," until their Rebuttal and, when asked about this new justification, Applicants' witness was unable to identify, quantify, or specify where in Applicants' testimony these new projects could be found.[112]

Applicants still have not identified where in the record evidence these "new capital expenditures" that DRA did not take into account can be found. Applicants' repetition of their previously unsubstantiated rebuttal testimony

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[110] Sempra Opening Brief, p. 214, lines 19 - 20.

[111] Sempra Opening Brief, p. 214, lines 21- 22.

[112] Q: "You refer to growth in [new] capital expenditures as a justification for the 3.3 incremental full-time equivalent employees SDG&E is seeking. And you disagree with DRA's conclusion that the growth in new capital expenditures for SDG&E has already largely taken place, saying that maybe DRA did not take all of the capital expenditures into account because many of these projects are approved in separate filings rather than the GRC; do you see that?" A: Correct. Q: Did you identify what you're referring to as these projects that are approved in separate filings in your GRC testimony or workpapers? A: Have I identified them specifically? Q: Did you in your – the initial GRC testimony and workpapers? A: No, I did not. Q: And have you in the rebuttal testimony? A: Not specifically. Q: At lines 13 and 14 where you say that SDG&E's total capital expenditures are forecasted to triple in 2008, do you know what the total capital expenses in 2006 were versus 2005? A: I don't have those exact figures in my head. Q: Do you have an approximate idea? A: This would be completely a guess. I think it's in the 500 – to 600 –million-dollar range. Actually, to tell you the truth, I can't tell you if I have the number in my head for both utilities or just SDG&E. Since you are asking about SDG&E only, I'd like to just defer. Q: Defer to someone else or just don't know? A: Defer answering the questions. Q: So the answer is you don't know? A: That's right." (10 RT 908-909, Kyle/ SDG&E/SCG.)

provides no factual basis for their increase request. DRA continues to recommend that the Commission reject it.

15. Corporate Center Costs Allocated to Utilities

In DRA's Opening Brief, DRA addresses most of the arguments the Applicants make for allocating certain Corporate Center Costs to the Utilities.[113] Below, DRA addresses a new argument made by Applicants in the area of Communications and Investor Relations (IR).

15.1 Communications and IR

In its Opening Brief, DRA recommended $0 ratepayer funding for the Corporate Center Communications and IR department because of duplication of functions with the Utilities.[114]

In their Opening Brief, Applicants quote from the cross examination testimony of DRA's Corporate Center witness responding to questions about whether "Utilities perform communications with stock analysts."[115] According to Applicants, since DRA's witness agreed that "it appears that [the Utilities] may not perform those same functions,"[116] this "thus completely nullif[ies] DRA's requested $3.124 million disallowance."[117]

DRA disagrees and continues to recommend that the entire $3.124 million be disallowed. As DRA noted in its Opening Brief,[118] the description Applicants gave of the functions of Corporate Center's Communications and IR department is not limited to the one sentence in the lengthy data request that Applicants describe as communicating with "stock analysts."

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[113] DRA Opening Brief, pp. 286 – 328.
[114] DRA Opening Brief, p. 290 – 291.
[115] 17 RT 2206, line 10 to 2207, line 27, Bower/DRA.
[116] 17 RT 2207, line 23-24, Bower/ DRA.
[117] Sempra Opening Brief, p. 219.
[118] DRA Opening Brief, pp. 289-292.

In any case, with or without duplication, DRA does not agree that Applicants have met their burden of proving that this function should be charged to ratepayers. The actual language Applicants used to describe the Investor Relations department is the following: "Investor Relations is a corporate department responsible for communicating with analysts, portfolio managers and other members of the financial community regarding Sempra Energy and its subsidiaries."[119] "Sempra Energy and its subsidiaries" includes numerous unregulated entities, and ratepayers should not be held responsible for costs incurred for those unregulated entities. Since Applicants have provided no information showing what portion, if any, of the Investor Relations charges actually relate to the *regulated* utilities, DRA continues to recommend $0 ratepayer funding for the entire department.

16. Shared Services and Assets

In DRA's Opening Brief, DRA addresses most of the arguments the Applicants make for allocating Shared Services costs.[120] Below, DRA addresses only the new arguments Applicants make in their Opening Brief in the areas of Customer Services Information (SDG&E) and for costs related to various of the Utilities' Regional Public Affairs cost centers.

16.1 A&G

DRA addresses these issues in its Opening Brief at pages 330-336.

16.2 Support Services

DRA proposed no adjustments in this area.

16.3 Emergency Preparedness

DRA addresses these issues in its Opening Brief at pages 336-338.

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[119] Ex. 275.

[120] DRA Opening Brief, pp.328-363.

16.4 Customer Services Information (SCG)

DRA addresses these issues in its Opening Brief at pages 338- 339.

16.5 Customer Services Information (SDG&E)

For Customer Services Information (SDG&E), Applicants propose an increase over 2005 recorded adjusted costs. In the course of DRA's Audit, however, DRA discovered $1.891 million in 2005 recorded data for costs relating to a customer information program and the company logo that should be removed before forecasting the test year expenses. As DRA describes in its Opening Brief, neither of these programs should be funded by ratepayers.[121]

The 2005 costs for the customer information program include materials to address customer concerns about the energy crisis and rolling blackouts.[122] Since the energy crisis was a specific situation not expected to be repeated, DRA removed these costs.

In its Opening Brief, Applicants argue that "…the energy crisis has led to continuous news coverage on grid conditions and potential for rolling blackouts…" and make reference to a Restricted Maintenance Alert issued by the CAISO in July 2007.[123] Applicants have provided no verifiable data showing any link between news alerts issued by the CAISO and SDG&E's expenditures. Applicants still have not met their burden of proving their claim is reasonable.

In DRA's testimony, DRA also noted that other materials in the customer information program had the characteristics of institutional advertising.[124] In their Opening Brief, Applicants offer their own definition of "institutional advertising," with no citation, and then characterize the content of a DRA data response, also

[121] DRA Opening Brief, pp.339-342.
[122] Ex. DRA-41, p. 41-5.
[123] Sempra Opening Brief, p. 258.
[124] Ex. DRA-41, pp. 41-15 – 41-16.

without a citation, that does not seem to be in the record. Applicants' arguments are all beside the point.

At one time or another, it seems that nearly every industry the Commission regulates has attempted to burden its ratepayers with the costs of institutional advertising.[125] Over the years, the Commission has defined "institutional advertising" as advertising that promotes "...goodwill to the company"[126] and advertising "... to enhance the general corporate image."[127] The long-standing Commission policy has been to disallow costs "...for corporate advertising other than advertising relating to safety, conservation and certain financial issues."[128]

As noted in DRA's Opening Brief, the advertisements Applicants use as examples of their "informational" activities do not inform customers of safety, conservation or financial issues, they merely tout Sempra as the provider of "clean renewable resources." Applicants have failed to show why the Commission should make an exception for them and require their ratepayers to fund their self-serving image enhancement campaigns.

As with the "customer information program," DRA's Auditors also recommend that the costs associated with the company logo should be disallowed as "institutional advertising." Applicants' argument in their Rebuttal, echoed in their Opening Brief, is that the costs incurred in connection with the logo were not "institutional advertising," but were incurred to avoid "customer confusion." Applicants offered no objective evidence to support this belated justification and DRA continues to recommend that these costs also be removed from the base year.

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[125] Re SCE (1996) 64 CPUC 2d 241, 325,D.96-01-011. *See also* Application of Pacific Gas and Electric Company (1989) 32 CPUC 2d 500, 504, D.89-09-094; In the Matter of the Application of California Water Service Company (2003) D.03-09-021, mimeo, p. 43.

[126] Re Roseville Telephone Company (1996) 70 CPUC 2d 88, 136, D.96-12-074.

[127] *See e.g.,* Pacific Telephone & Telegraph (1974) 77 CPUC 117, 156, D.83162

[128] Joint Application of Pacific Enterprises, Enova Corporation, et al. for Approval of a Plan of Merger (1998) 79 CPUC 2d 343, 372-373, D.98-03-073 citing Re SoCalEdison (1976) 81 CPUC 49, Re PG&E (1975) 78 CPUC 638, 691-696.

16.6 Customer Services Operations (SCG)

DRA addresses Applicants' arguments in this area in DRA's Opening Brief at pages 341-342.

16.7 Customer Services Operations (SDG&E)

DRA does not dispute the Applicants' forecasts in this area.

16.8 Engineering

DRA does not dispute the Applicants' forecasts in this area.

16.9 Gas Distribution

16.9.1 Regional Public Affairs

In its Opening Brief, in both this section and in numerous others, Applicants argue that ratepayers should fund their Regional Public Affairs departments. To justify this, Applicants offer anecdotal tales of instances where the Regional Public Affairs personnel met with public officials to "decrease the inconvenience of street closures," "increase public safety," and "reduce[] operational costs."[129]

In its Opening Brief, DRA has already addressed the underlying Commission precedent and policy generally barring ratepayer funding of exactly the activities these departments perform.[130] The Commission has clearly stated that the burden is on the Applicants "... to demonstrate a delineation of the costs." The Sempra Utilities have not done so.

For all their stories of meeting with Public Works directors to "avoid removal and re-paving conditions"[131] or intervening "[w]hen the North County Transit District alleged that SDG&E wasn't paying certain easement fees,"[132] the

[129] *See e.g.,* Sempra Opening Brief, pp. 270, lines 13-18.
[130] See e.g., DRA Opening Brief, pp. 343-347.
[131] Sempra Opening Brief, p. 263, lines 22-26,
[132] Sempra Opening Brief, p. 270.

Applicants have not provided any verifiable evidence of how much time their Regional Public Affairs departments spent on these activities, or when, as opposed to how much time they spent attempting to influence the decisions of public officials. Based on Applicants' failure to meet their burden of proof, DRA continues to recommend $0 ratepayer funding for the RPAs.

16.10 Gas Transmission

DRA does not dispute the Utilities' forecast in this area.

16.11 Electric Distribution

DRA addresses Applicants' arguments in this area in DRA's Opening Brief at pages 345 – 347.

16.12 Corporate Center Re-allocation

DRA addresses this subject in DRA's Opening Brief at pages 347- 356.

16.13 Shared Service Database

DRA agrees that the list of enhancements to the Shared Service Database that Applicants include in their Opening Brief accurately represents DRA's proposals.[133] DRA looks forward to working with Applicants to produce the version of this database and the RO model that will be used in the next GRC.

17. Employee Issues (generic employee-related issues)

In its Opening Brief, DRA addresses most of the arguments Applicants make regarding Employee Issues. Below, DRA addresses three areas: the "purpose" of the Total Compensation Study reports, and recurring factual errors about DRA's Medical Plan and Employee Assistance Plan recommendations.

17.1 2008 Staffing Levels

DRA addresses Applicants' arguments on this issue in DRA's Opening Brief at pages 363-366.

[133] See Sempra Opening Brief, pp. 272-273.

17.2 Compensation and Benefits

In their Opening Brief, Applicants state that "[t]he purpose of the [Total Compensation Study] reports was to determine if total compensation, including incentive compensation pay (ICP) is reasonable for ratemaking purposes."[134] While that may be the Applicants' interpretation of the purpose of the studies, it is not DRA's.

The findings of the Total Compensation Studies do not dictate whether Applicants' proposals for total compensation are reasonable. They provide one analysis of Applicants' market position with regard to base pay, short term incentive compensation, benefits, long term incentives and total compensation.[135] The reports do not substitute for the Commission's own judgment of whether each of these component parts is just and reasonable for ratepayers to fund.

In fact, as discussed in DRA's testimony and Opening Brief, it would be absolutely *un*reasonable to adopt Applicants' requests for compensation and benefits as proposed. Applicants' requests are based on forecasts that are inconsistent and/or unsubstantiated, and are inflated with expenses and supererogatory perquisites that the Commission has disallowed in numerous other GRC decisions.

17.2.1 SoCalGas

Medical Plans

In their Opening Brief, Applicants argue that "DRA ignored the actual medical premium rate increases for 2006 and 2007."[136] Applicants provide no citation for this statement which is factually incorrect. As DRA noted in its testimony, with citations to the data requests responses from the Applicants, DRA's forecasts for medical expenses use Applicants' 2006 actual medical

[134] Sempra Opening Brief, p. 285.

[135] *See e.g.,* Ex. SDG&E-13, Total Compensation Study, p. 8, 14-19.

[136] Sempra Opening Brief, p. 277.

expenses.[137] DRA did not "derive" its escalation rate; DRA calculated the rate based on the actual medical expenses the Utilities provided.

With regard to Medical Plan expenses, Applicants' recorded expense data shows an average annual inflation rate of about 8%[138]. Even the Utilities agree that, "[b]ased on the latest rate forecasts provided by Towers Perrin, annual increases are projected to gradually decrease from approximately 9.0% to 7.0% over the long-term."[139] In addition, Global Insight, which the Utilities used to forecast various other expense levels for the test year, shows a rate increase for Group Health Insurance of 5.0% for 2007 and 4.3% for 2008.[140] Despite this evidence, Applicants persist in seeking an increase that is based on the largest possible increase in headcount numbers and the highest inflation rates referenced by the actuaries.[141] DRA notes that the end result of Applicants' method for SDG&E, for example, would be an increase of 16.70% from 2005 to 2006, and a 17.26% increase from 2006 to 2007 for medical expenses.[142] Applicants' justification for these monumental increases rests on ever shifting forecasts of headcounts, and forecasts that cannot be reconciled with the workpapers that are supposed to support them.[143] Applicants' showing falls so far short of approaching the burden of proof, that this area, too, should be a non-issue.

Employee Assistance Plan

In their Opening Brief, Applicants argue that "…DRA's proposal would result in a significant disallowance for the mental health benefits" and say that

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[137] Ex. DRA-35, p. 35-10; Ex. DRA-14, p. 14-10, footnote 22.

[138] 7.99% in 2006 for SCG (Ex. DRA-35, 35-10) and 8.09% for SDG&E (Ex. DRA-14, p. 14-9).

[139] Ex. SDG&E-13-E, p. GJR/JAH-18, lines 1 -4.

[140] Ex. DRA-14, p. 14-11, footnote 23.

[141] See 17 RT 2128, lines 5-28, Godfrey/DRA.

[142] Ex. DRA-14, p. 14-10.

[143] 17 RT 2128- 2129, Godfrey/ DRA.

"DRA excluded mental health claims from EAP expense from SCG while allowing it at SDG&E."[144]

Applicants then present the convoluted trail of the inconsistent, contradictory, and inaccurate information Applicants have provided DRA on this subject. By DRA's count, Applicants provided three different estimates of their forecast for SCG's EAP expenses, and five different estimates of their forecast of SDG&E's EAP expenses, the last one being provided by Applicants on the witness stand.

Applicants claim that "while it is unfortunate that this error is made, there is no reason to continue to carry this forward when setting the 2008 revenue requirement."[145] DRA disagrees. Applicants' ever-shifting, never-substantiated showing on this issue utterly fails to meet the burden of proof. There is no factual basis for the Commission to adopt Applicants' EAP forecasts and DRA continues to recommend that the Commission adopt DRA's proposals.[146]

17.2.2. SDG&E

DRA's recommendations on issues relating to SDG&E's Employee Compensation and Benefits are discussed in DRA's Opening Brief at pages 395-426.

17.3 Diversity

DRA has no comment on this issue.

17.4 Pensions

DRA addressed the Sempra pension proposals in its Opening Brief. In its discussion of Supplemental Pension & IRC Section 415 plans, Sempra states, "Attracting and retaining employees at all levels is essential to maintaining quality

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[144] Sempra Opening Brief, p. 279.

[145] Sempra Opening Brief, p. 279.

[146] Ex. DRA-35, p. 35-17; Ex. DRA-14, p. 14-7

service and reliability for all ratepayers. DRA's witness even agreed to this point."[147] Sempra provides no citation for this statement and did not even cross examine the DRA pension witness. While DRA agrees with the above statement in the abstract, DRA's testimony disputed that these plans should be funded by ratepayers. In discussing the Section 415 plan, DRA noted:

> As with supplemental pension benefits, SoCalGas has not demonstrated that these enhanced benefits are necessary for it to attract and retain skilled employees or supported the reasonableness of ratepayer funding for the costs associated with supplemental benefits beyond traditional funding levels and limitations.[148]

DRA's opposition to ratepayer funding for the Supplemental Pension and Section 415 plans is clearly explained in its testimony. Most pertinently, Sempra's Total Compensation Studies showed that executive benefits are at or above market, and that total executive compensation is considerably above market (32% for SDG&E, 65% for SoCal), *even without counting supplemental pension benefits*.[149] In its Opening Brief, Sempra states, "Motivating and retaining a top-quality, experienced leadership team requires a competitive compensation and benefits package."[150] Yet Sempra's own studies show that its executive compensation package is already more than competitive. Sempra is free to continue offering these benefits at shareholder expense, if it chooses, but ratepayers should not be made to pay the cost of benefits that surpass competitive levels.

Sempra also argues that, "The Excess Cash Balance Plan and Section 415 Excess Plan are designed to maintain the same benefit level, on a percentage basis,

[147] Sempra Opening Brief, p.294.
[148] Ex. DRA-27, p.27-9.
[149] Ex. DRA-15, p. 15-7, Ex. DRA-27, p. 15-6
[150] Sempra Opening Brief, p.294.

as provided in Applicants' broad-based Cash Balance and Savings plans."[151] This is not evidence of reasonableness, and it does not answer the question of whether ratepayers ought to bear the cost of the benefits. The relevant facts are that these supplemental-pension benefits exceed the limits specified by IRS regulations and by ERISA,[152] and that Sempra's total executive compensation is well above competitive levels. For these reasons, the Commission should the exclude the costs of supplemental pensions when it sets the revenue requirements for SoCal and SDG&E.

17.5 PBOPs

DRA discusses this issue above in Section 3.10 and in its Opening Brief at pages 439-440.

18. Ratebase

18.1 Common Issues

DRA's company specific recommendations on ratebase are addressed in DRA's Opening Brief at pages 449-452. Below, DRA addresses the Applicants' opposition to DRA's calculations and methodology that applies equally to both SCG and SDG&E.

18.2 Working Cash

SCG and SDG&E oppose the DRA's methodology underlying its recommendations for Cash Balances, Revenue lag days, FIT and CCFT lag days, and accrued vacation, all which affect the working cash balances.

18.2.1 Cash Balances

DRA recommends that both SDG&E and SCG cash balances be reduced to $0 because SP U-16 only allows minimum bank deposits for cash balances. The Applicants oppose this recommendation and argue that they are entitled to be

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[151] *id*.

[152] Ex. SCG-11, pp. GJR/JAH 37, Ex. SDG&E-13, pp. GJR/JAH 37-38.

reimbursed for reasonable amounts of working funds in addition to the minimum bank deposits.[153] The Applicants base their argument on an erroneous interpretation of SP U-16. SP U-16 states that Cash Balances include minimum bank deposits that are reasonable amounts of working funds. The Applicants err in arguing that SP U-16 allows minimum bank deposits and, in addition, reasonable amounts of working funds.

There are two sentences in SP U-16 that supports DRA's interpretation. The first sentence states:

> "In determining the cash requirement, the only amounts which should be considered are the required minimum bank deposits that must be maintained and reasonable amounts of working funds."[154]

While at first glance, that particular sentence may seem to support the Applicants' contention because the word "and" is used ambiguously, i.e. it can mean "or" as well, the following sentence in the same paragraph negates the Applicants' interpretation:

> "if the funds were to be allowed in the cash requirement, over and above the minimum bank deposits for payment of certain operating expenses, it would have the effect of providing for payments of the same cost twice.[155]"

The sentence above clearly limits cash balances to only "minimum bank deposits," and not minimum bank deposits OR reasonable amounts of working funds. SP U-16 unambiguously states that any funds "over and above the minimum bank deposits" should not be counted within cash balances. The

[153] Sempra Opening Brief, p. 298.
[154] Exh. DRA-55, p.1-4, paragraph 11.
[155] *Id*.

Applicants' interpretation would be correct *only* if SP U-16 would have read "over and above the minimum bank deposits AND reasonable amounts of working funds." However, that sentence only includes "minimum bank deposits" and nothing else.

There should be no question that only *minimum bank deposits that are reasonable working funds* are allowed in cash balances. Since the Applicants state that their banks do not require minimum bank deposits, the Commission should set cash balances for both utilities at $0. DRA's position is further supported by the fact that the Commission adopted cash balances for both SCE's and PG&E's prior GRCs were set at $0.[156] Obviously, SCE and PG&E needed reasonable amounts of working funds and the Commission would have granted them with such funds in their cash balances if the Applicants were entitled to recover costs. However, the Commission adopted $0 for cash balances because SCE and PG&E banks did not require a minimum bank balance.

18.2.2 Lead Lag Days

The Applicants oppose DRA's recommendation to calculate lead lag days based on a five-year average forecast. They propose that the Commission instead forecast lead lag days based on actual 2005 recorded data.[157]

The Applicants state that "if the weighted averages in the study include data from different timeframes, the study as a whole is rendered mathematically flawed."[158] The Applicants mischaracterize DRA's position by implying that DRA somehow mixes and matches data from different years. This is simply incorrect; DRA compiled all data that the Applicants provided from 2001-2006 and took the five-year average to compute the lead lag days. Since the Applicants'

[156] Application of Southern California Edison Company for General Rate Increase (2004) D.04-07-022; 2004 Cal.PUC LEXIS 325; Application of Pacific Gas and Electric Company for General Rate Increase, (2007) D.07-03-044, 2007 Cal. PUC LEXIS 173.

[157] Sempra Opening Brief, p.302 and p.308.

[158] Sempra Opening Brief, p. 296: lines 15-18.

premise is incorrect, this argument is irrelevant and should be rejected on that basis.

The Applicants provide vague and unsupported allegations that DRA's five-year average forecast is contrary to SP U-16 because a five-year forecast is not a "consistent timeframe.[159]" The Applicants unnecessarily limit the meaning of "consistent timeframe" to data from one year. DRA agrees that the lead-lag calculation should be based on a consistent timeframe, and a consistent timeframe can consist of an average number. The Commission has adopted five-year averages for GRCs in the past and therefore the Applicants' position that "consistent timeframe" cannot include five-year averages is unfounded.[160]

DRA's and the Applicants' forecasts are very similar. SCG's revenue lag day forecast is 42.36 days while DRA's forecast is 40.26 days. And, SDG&E's forecast is 38.04 while DRA's forecast is 37.44. DRA takes the average of 2002-2006, while the Applicants use only 2005 data. The Commission has indicated that five-year averages are more reliable than the use of a single year's data.[161] DRA's forecast follows that direction and DRA recommends that the Commission adopt it.

18.2.3 FIT and CCFT

The Applicants oppose DRA's FIT and CCFT lag day calculation because DRA uses an annual service midpoint. The service midpoint is an important factor used to calculate FIT and CCFT lag days.[162] The Applicants incorrectly calculate FIT and CCFT lag days based on a quarterly service midpoint.[163]

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[159] Sempra Opening Brief, p. 296.h

[160] Re: PG&E (1986) D.86-12-095, 1986 Cal. PUC LEXIS 886, *277.

[161] Re: SCE (2004) D.04-07-022; 2004 Cal. PUC LEXIS 325, *27.

[162] Exh. DRA-38, p.38-6.

[163] *Id*.

The evidence in the record in this case establishes that SCG's and SDG&E's tax payments to Sempra are annualized and therefore the service midpoints should be based on annual payments. The Applicants incorrectly state that "SDG&E is required by the IRS to make four estimated quarterly tax payments during each calendar year."[164] SDG&E and SCG are not required to make any tax payments directly to the IRS because Sempra makes tax payments on their behalf.[165] And, the tax payments transferred to Sempra are a function of an annualized formula.[166] In its own report, titled "San Diego and Electric Cash Working Capital Study Test Year 2004,[167]" SDG&E calculated service mid-points to be each July.[168] Therefore, SDG&E is contradicting itself when it says that it calculates quarterly service periods.

The applicants state that DRA's use of mid-year service points "does not mirror the applicable tax laws."[169] SDG&E confuses tax law with regulatory law. DRA is not attempting to mirror applicable tax laws, but applies long-standing Commission methodology and Applicants' actual tax payment date to calculate the FIT and CCFT lag days. Tax laws are irrelevant to calculate the FIT and CCFT lag days.

DRA's methodology was utilized by SCE in its TY 2006 GRC and by PG&E in its TY GRC.[170] PG&E and SCE, like SCG and SDG&E, are owned by parent corporations and do not make direct tax payments to the IRS. PG&E and SCE make payments in the same manner as SCG and SDG&E. The Commission

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[164] Sempra Opening Brief, p. 303.
[165] Exh. DRA-53.
[166] *Id*.
[167] *See* Exh. DRA-56.
[168] 10 TR 989, SDG&E/Kyle lines 17-30.
[169] Sempra Opening Brief, p. 303: lines 17-18.
[170] Exh DRA-38, p. 38-7.

has calculated these tax payment lag days annually.[171] SDG&E's witness, Mr. Kyle, stated that he is not specifically aware of how the Commission has been calculating FIT and CCFT lag days for the past few GRCs.[172] Instead of focusing on tax laws to calculate this regulatory specific formula, DRA's calculations are based on how the Commission calculates FIT and CCFT lag days. DRA recommends that the Commission adopt DRA's proposals.

18.2.4 Adjustment for Accrued Vacation

The Applicants deny that their vacation accrual accounts are cash accounts. This is factually incorrect; Applicants admit that they have to pay each employee for 2080 hours per year, regardless of whether employees take their vacation.[173] There is no doubt that ratepayers pay each employee for 2080 hours, which includes vacation time, yet the Applicants continue to deny that ratepayers fund accrued vacation.

Based on SP U-16 and Commission precedent, accrued vacation should be deducted from the Utilities' working cash.

18.3 SCG Issues

See section 18.2 above and DRA's Opening Brief for DRA's working cash recommendations for SCG.

18.4 SDG&E Issues

See section 18.2 above and DRA's Opening Brief for DRA's working cash recommendations for SDG&E.

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[171] *Id.*

[172] 10 TR 986 SDG&E/Kyle lines 20-24.

[173] Exh SDG&E 228, p.13, lines 21-25.

18.4.1 Remove $514,000 from Fuel-in-Storage

The Commission should reject SDG&E's arguments that DRA erroneously removes fuel in storage from ratebase.[174] DRA's recommendation that fuel-in-storage be removed from ratebase is supported by the evidence in this record and Commission precedent.

SDG&E asserts that it has been authorized to include fuel in storage in rate base going back to at least its 1982 GRC, D.93892.[175] However, shortly after SDG&E's 1982 GRC, the Commission established the Energy Cost Adjustment Clause (ECAC now ERRA) mechanism to provide an industry-wide mechanism to provide public utilities with yearly recovery of fuel costs for electric operation. In fact, SDG&E filed its ECAC application, A.84-07-027, to revise its 1982 GRC decision, D. 93892, specifically addressing fuel inventory recovery.[176] The Commission resolved that application and adopted SDG&E's fuel inventory recoverable under ECAC.[177] Since that time, SDG&E has recovered its fuel costs under ECAC or subsequent proceedings. For example, in 1995, SDG&E filed its ECAC application requesting recovery of its fuel inventory costs. The Commission resolved that application in D.96-06-033 by granted reasonableness of SDG&E's fuel inventory case under its ECAC application.

In D.96-01-011, the Commission concluded that fuel inventory reasonable should not be determined in GRCs.[178] In D.06-05-016, the Commission refused to include SCE's fuel inventory in ratebase and stated:

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[174] Sempra Opening Brief, p. 311

[175] *Id.*

[176] Re San Diego Gas & Electric Company (1984) 16 CPUC2d 618, D.84-12-065,1984 Cal. PUC LEXIS 1048.

[177] *Id.* at *3.

[178] 1996 Cal. PUC LEXIS 23 at *76

> "We are not persuaded to change the current ratemaking treatment for fuel inventory**.** There is a long history to this issue.[179]"

The Commission's long standing policy is to exclude recovery of fuel inventory from ratebase. DRA's recommendation is consistent with Commission policy and should be adopted.

19. Depreciation

19.1 Common Issues

19.1.1 Net Salvage

DRA's Net Salvage Analysis Is Reasonable And based On Both Objective And Subjective Criteria

The Utilities' Opening Brief seeks to validate its proposed net salvage rates based on the use of the 15-year historical average. Applicants' brief states, "Where appropriate, Applicants also considered (1) historical trends of company data, (2) currently-authorized levels of future net salvage, and (3) average rates of the industry and other CPUC-regulated utilities."[180] Applicants repeat these additional factors in an attempt to demonstrate the supposed contradictory testimony by DRA's witness, Bernard Ayanruoh where Mr. Ayanruoh states that the "... Sempra Utilities are the only utilities that I know that [do] not even look at industry statistics."[181]. However, DRA found no evidence in the Applicants' prepared testimony indicating that they did consider historical trends, currently-authorized levels of net salvage, average rates of the industry, or other CPUC-regulated utilities. Only in rebuttal testimony do Applicants make an effort to describe these additional considerations. Contrary to Applicants' assertion that "company-specific data was given the greatest weight,"[182] based on the proffered

[179] 2006 Cal. PUC LEXIS 189 at *399

[180] Sempra Opening Brief, p. 315, lines 10-12.

[181] Sempra Opening Brief, p.316, lines 7- 8.

[182] Sempra Opening Brief, p. 315, line 12.

evidence entered on the record, it would seem company-specific data was the *only* factor taken into account in the net salvage analysis.

Applicants' Opening Brief attempts to color DRA's net salvage analysis, calling it "one-sided," "subjective," and "arbitrary."[183] Applicants assert DRA's adjustments to the proposed net salvage rates "... reveals a one-sided bias toward smaller net salvage rates and use of inconsistent approaches."[184] DRA disagrees that its approach was inconsistent. However, DRA does agree that its analysis includes an element of bias,[185] as is expected in any forecast. During evidentiary hearings, Applicants' witness, Rodger Larsen, testified to this effect:

> [DRA] Q So would you agree that the determination of depreciation parameters such as the service lives and net salvage rates is a very subjective area?
>
> [Mr. Larsen] A Service lives in particular I would say are a subjective area. Other parameters can be.
>
> Q What about net salvage rates?
>
> A Well, actually, that's an instance where I attempted to remove some subjectivity by starting with a uniform 15-year band, and companies have used that historically. And also I was influenced to make that subjective decision to use 15-year band by DRA's position, as I note in footnote 1, regarding the SCE, I guess it would be 2005 GRC. DRA was adamant that 15 years was the superior band which the company should use, listing, I believe, four reasons.
>
> Q Do you agree that net salvage rate is a forecast?
>
> A Yes, it is.
>
> Q So as with any other forecast, would you agree that two separate analysts could use identical data to perform a net salvage analysis and come up with different conclusions?

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[183] Sempra Opening Brief, p. 315, line 19.

[184] Sempra Opening Brief, p. 315, lines 26-27.

[185] DRA Opening Brief, p. 454.

A Certainly.[186]

Applicants' Opening Brief offers no new arguments on this issue. DRA's Opening Brief addresses the arguments raised by Applicants, explaining in an account-by-account analysis the support for the recommended adjustments.[187] DRA's analysis illustrates that Applicants' presumed "comprehensive and balanced approach"[188] is in fact predisposed to an over-reliance on 15-year historical data, which can often produce uneven results if other factors (such as those enumerated above) are not given full consideration.

DRA's Reporting Requirements Have Been Adopted By The Commission In Other GRCS

Applicants' Opening Brief states "there is no basis to support the need for additional costly reporting requirements."[189] DRA disagrees since the Commission has adopted this reporting requirement in other GRC proceedings. DRA's Opening Brief addresses the arguments raised by Applicants at pages 477-479.

19.2 SoCalGas Issues

DRA discusses these issues in its Opening Brief at pages 449-465.

19.3 SDG&E Issues

DRA discusses these issues in its Opening Brief at pages 465- 477.

20. Taxes

DRA discusses taxes at pages 479-481 of its Opening Brief.

21. Miscellaneous Revenues

DRA addresses these issues at pages 481-483 in its Opening Brief.

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[186] Tr. Vol. 7, p.516, line 24 – p.517, line 18.
[187] DRA Opening Brief, pp. 456-477.
[188] Sempra Opening Brief, p. 317, line 4.
[189] Sempra Opening Brief, p. 318, lines 28-29.

22. Sales and Customers

DRA addresses these issues at pages 481-484 in its Opening Brief.

23. Regulatory Accounts

DRA addresses these issues at pages 484-489 of its Opening Brief.

24. Escalation

DRA does not dispute the utilities' proposed escalation factors and methodologies for this rate case.

25. Audit & Accounting Issues

DRA's Audit findings and recommendations are discussed in DRA's Opening Brief at pages 492-495 and in this Reply Brief in Section 16.5.

26. Summary of Earnings/Results of Operations Model

26.1 Common Issues

26.1.1 Tracking Ratemaking Adjustments Module

In GRCs, the revenue requirements are calculated by a computer model which is referred to as the Results of Operations (RO) model.[190] The RO model that the Applicants provided with their December 2006 application was essentially the same as the RO model Applicants used in their 2004 Cost of Service proceeding, but for this case, Applicants added two new features. The first is an automated labor loader that adjusts costs for employee benefits, incentive programs, and payroll taxes as direct labor changes. The second new feature is a database which is used to forecast the cost of Shared Services billed from one utility to the other.[191]

DRA used the Applicants' RO model to input DRA witness recommendations[192]. In some instances, to reflect the DRA witness

[190] Ex. DRA-28, p. 1.

[191] *See, e.g.,* Ex. DRA-28, p. 28-2.

[192] With the exception of DRA's Shared Service adjustments which were made to the Shared Service Database directly.

recommendations, DRA made changes in various cells in the RO model.[193] After DRA's testimony was served, DRA provided Applicants with an updated Summary of Earnings/ Revenue Requirement tables to include corrections to conform the DRA tables to the latest recommendations of the DRA witnesses.[194]

In their Opening Brief, Applicants present a long and involved argument about DRA's use of the Applicants' RO model.[195] The premise of Applicants' argument appears to be DRA-3, a data request response from DRA to the Applicants which is not part of the record. Applicants characterize and offer partial quotations from that data response, but as the data request response is not in the record, these statements are not evidence. The Public Utilities Code requires the Commission to base its findings on "substantial evidence in light of the whole record."[196] Applicants' allegations are outside the record and cannot, therefore, form the basis of any Commission findings.

In their Opening Brief, Applicants also criticize DRA for not "correcting" the labor overheads for their Incentive Compensation Plan (ICP).[197] DRA made its changes to the RO model to reflect DRA witness recommendations which differ from the Applicants in numerous areas, ICP among them.

What is clear from the record evidence is that when the Applicants' provided DRA with the RO model, that model contained logic flaws.[198] DRA attempted to correct the logic flaws and, in fact, discussed those flaws and other corrections with a member of the Applicants' staff. [199] In their Opening Brief,

[193] Ex. DRA-28, p. 2.
[194] 16 RT 1984- 1986, Jarjoura/DRA.
[195] Sempra Opening Brief, p. 371-373.
[196] Public Utilities Code Section 1757(a)(4).
[197] Sempra Opening Brief, p. 372.
[198] 11 RT 1056-1057, Yee/ SDG&E/SCG.
[199] 11 RT 1057, Yee/SDG&E/SCG

Applicants recommend that all changes any other party makes to their model "... be supported in written testimony."[200] This recommendation should be rejected since it is based entirely on non-record allegations.

In addition to being unjustified, Applicants' proposal is also unnecessary. As noted *on* the record, a change log module will track changes to the model at a cost of approximately $200,000.[201] Applicants had the option to purchase that feature, but declined it for budget reasons. DRA recommends that the Applicants set aside that sum from the revenue requirement they are ultimately authorized in this case and purchase the change log option.

26.2. SoCalGas Issues

In their Opening Brief, Applicants state that DRA "....incorrectly assumed they could include PBOP amortization in miscellaneous revenues."[202] This is not an RO model issue; this is a difference of opinion relating to how the PBOPs overcollection should be returned to ratepayers.

Applicants' witness testified that she "...[did not] think it should be accounted for in the RO model." In her opinion, "… a collection of a prior year over/ undercollection was treated separately in our ratemaking and not in the test year base margin or miscellaneous revenues."[203] DRA disagrees.

DRA's recommendation, explained in Section 23 of its Opening Brief, is that "...the overcollection be amortized over the period that the rates in this GRC are in effect (i.e., the five-year GRC cycle proposed by DRA), and captured in the revenue requirement determination. DRA makes this recommendation because of the magnitude of the PBOPs balancing account overcollection.[204] DRA's change

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[200] Sempra Opening Brief, p. 373.

[201] 11 RT 1062, Yee/ SDG&E/SCG.

[202] Sempra Opening Brief, p. 372.

[203] 11 RT 1059, lines 4-9, Yee/ SDG&E/SCG

[204] DRA Opening Brief, p. 486.

to the RO model for the PBOP amortization reflects the impact on the revenue requirement of DRA's recommendation.

26.3 SDG&E Issues

In their Opening Brief, Applicants argue that "DRA appears to have improperly assumed that they could combine multiple CapEx functions into one single project adjustment."[205] This argument is in reference to a reduction DRA made to the RO model to reflect the difference between what SDG&E forecasted for its 2006 capital expenditures in the areas addressed in other DRA Exhibits[206] and what the Utility actually spent in 2006. The difference is $0.561 million.[207]

Because SDG&E did not update its RO model to reflect this difference, DRA did so itself using IT capital expenditures as a proxy. In reflecting DRA's recommended adjustments for IT, as set forth in Exhibit DRA-17, DRA had already modified the RO model to incorporate 2006 IT capital changes. By making the additional $0.561 million reduction, the RO model correctly reflects SDG&E's actual recorded 2006 IT capital expenditures.[208]

According to Applicants, however, this change to the RO model "… generates incorrect depreciation, tax flow through, rate base, shared asset billing, which together will cause a misstatement of the revenue requirement."[209] Again, DRA disagrees. The magnitude of the proposed adjustment ($0.561 million in capital expenditures) means that the impact on the revenue requirement will be roughly $112,000.[210]

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[205] Sempra Opening Brief, p. 372.

[206] *See* Ex. DRA-6, DRA-7 and DRA-11.

[207] 13 RT 1505, lines 1-15, Wilson/DRA.

[208] 13 RT 1505, lines 16-23, Wilson/ DRA.

[209] Sempra Opening Brief, p. 373.

[210] Assuming all of the capital adjustments are reflected in rate base by 2008, a 10% rate of return coupled with a net to gross multiplier of 2 produces a rough revenue requirement impact of $112,000. Second order adjustments, such as depreciation, would

The purpose of DRA's adjustment was to reflect the principle that the most recently recorded capital expenditures should be incorporated in the RO model. No matter which IT projects were modified, or whether separate proxy adjustments were made for each of the DRA exhibits where IT adjustments were recommended, there is little opportunity for meaningful inaccuracies to occur, and those that might show up would pale in comparison to not reflecting the $0.561 million adjustment at all.

27. Post Test Year Revenue Requirement Issues

27.1 Term of Rates Adopted

DRA addresses this issue in its Opening Brief at pages 502- 505.

27.2 Use of Adjustment Indices for Base Rates

27.2.1 Capital-Related Cost Adjustment

Applicants' Opening Brief states, "[T]he Handy Whitman indexes are preferable to use in escalating recorded net plant additions to PTY dollars since this well-established method accounts for inflation specific to the type of plant additions the Applicants will be making during the post test year period."[211] Applicants argue,

> "The CPI does not provide any significant benefit in terms of being simpler, more streamlined, or more verifiable than the utility-specific measures of inflation. A competent analyst with DRA or an interested party could confirm annual calculations of the utility-specific inflation measure within a few hours, or one day at the most thorough level."[212]

DRA disputes the fact that the utility indexes are easily verified, and recommends use of the CPI-U as a more reliable indicator of inflation. DRA's

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have minor impacts on that figure.

[211] Sempra Opening Brief, p. 380, lines 31-34.

[212] Sempra Opening Brief, p. 384, lines 15-18.

Opening Brief addresses these arguments raised by Applicants at pages 506-507 and 509-511.

27.3 Measures of Inflation

DRA addresses this issue in its Opening Brief at page 509.

27.4 Indexing Methodology

DRA addresses this issue in its Opening Brief at pages 509-512.

27.5 Productivity

DRA addresses productivity factors in Section 27.8 below.

27.6 Z Factors

DRA addresses Z factors in its Opening Brief at page 515.

27.7 Earnings Sharing

27.7.1 DRA's Proposed Symmetrical Earnings Sharing Mechanism

DRA's Opening Brief already addresses the arguments raised by Applicants disputing DRA's proposed symmetrical earnings sharing mechanism.[213]

DRA's Opening Brief also already addresses arguments raised by Applicants regarding DRA's recommendation to narrow the deadband 0-25 basis points from 0-50, with a corresponding widening of Band 1 in the event a GRC cycle longer than three years is adopted by the Commission.[214]

27.7.2 Calculation of Ratepayer Portion ofEarnings Sharing -- Allocation of Tax Benefits

In the Opening Brief, Applicants assert shareholders, not ratepayers, have paid each utility's income taxes for earnings beyond authorized levels; therefore, the tax benefits associated with the ratepayer credit should be allocated between

[213] DRA Opening Brief, p. 515-19

[214] DRA Opening Brief, p. 518-19.

ratepayers and shareholders consistent with the sharing percentages under the utility's earnings sharing mechanism.[215]

DRA's Opening Brief already addresses the arguments raised by Applicants regarding the allocation of tax benefits.[216]

27.8 Utility of the Future Productivity Factors

In their Opening Brief, Applicants disagrees with DRA's proposal for a productivity factor of 1.3% in 2009 with a 0.2% stretch factor in subsequent years to account for UoF and other efficiencies.[217] DRA's Opening Brief already addresses most of Applicants' arguments.[218]

Applicants' Opening Brief, however, provides further arguments as to the uncertainty of whether the utilities can achieve the productivity targets planned in their PTY ratemaking proposals.[219] Applicants state, "Historically, in some years the utilities have been able to achieve their targets, in other they have not."[220] The brief further states, "[A]s time goes on, it becomes more and more difficult to develop those types of initiatives that can extract additional productivities out of the utilities' businesses."[221] But according to Applicants, UoF is intended to address this specific problem: UoF initiatives adopts "the willingness 'to see it through,' for the utilities to continue to create greater efficiencies in their processes and procedures."[222] Although Applicants maintain that anticipated

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[215] Sempra Opening Brief, p. 388, lines 27-31.
[216] DRA Opening Brief, p. 519-21.
[217] Sempra Opening Brief, p. 394, line 24.
[218] DRA Opening Brief, p. 512-14; p. 521-22.
[219] Sempra Opening Brief, p. 394, lines 31-32.
[220] Sempra Opening Brief, p. 394, line 32-33.
[221] Sempra Opening Brief, p. 395, lines 9-11.
[222] Sempra Opening Brief, p. 395, lines 29-30.

benefits from the productivity gain of UoF program remain uncertain, DRA continues to believe ratepayers should be able to capture some the potential incremental productivity gains from the UoF initiatives.

27.9 ALJ Questions

DRA has no comments regarding the ALJ questions.

27.10 Other Related Issues

27.10.1 Corporate Center Allocation Adjustment

DRA's Opening Brief already addresses arguments raised by Applicants regarding DRA's adjustment of $1.5 million to SCG PTY mechanism.[223]

28. Performance Incentive Mechanisms

DRA responds to the Applicants' Opening Brief discussing SCG's and SDG&E's issues relating to their respective performance incentive indicators. Performance incentives are relatively new ratemaking concepts for the Commission. The Commission began using performance incentives in 1994 for SDG&E and in 1998 for SCG.

The evidence in the record in this case establishes that SDG&E's and SCG's current performance incentive structures do not meet the main, underlying purpose for which the Commission first began using performance incentives -- to benefit ratepayers.[224] Performance incentives are supposed to be tools to lower costs, not raise them.[225] The current structure of performance incentives provides more rewards than necessary to SDG&E and SCG, meaning that ratepayers are paying more than necessary.[226] Applicants' Opening Brief suggests that they are somehow entitled to performance incentive rewards, like a fee or a tax. However,

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[223] DRA Opening Brief, pp. 507-9.
[224] 68 CPUC 2d 275, 290.
[225] 73 CPUC 2d 469, 490.
[226] *See* DRA Opening Brief, Section 28.

the Commission should reaffirm and clarify that performance incentives are meant to benefit ratepayers, and not shareholders.

Despite the ratepayer detriment that has resulted from the current performance incentives, DRA does not recommend that the Commission eliminate performance incentives or impose a penalty-only mechanism. DRA instead recommends that the Commission fix certain aspects of the current mechanism to achieve cost-effectiveness and increased performance levels. DRA's main recommendation to achieve this goal is that the Commission transition to an asymmetric performance incentives structure.[227] Naturally, because DRA's recommendation includes cutting down on unnecessary rewards, both Utilities oppose DRA's proposal by making exaggerated or factually incorrect arguments. DRA's responds to SCG and SDG&E's arguments, respectively, below.

28.1 Customer Satisfaction

28.1.1 Common Issues

The Applicants state that the Commission must adopt their proposals for Customer Satisfaction Incentives because they are necessary to achieve a certain level of service.[228] DRA has developed an approach that maintains that certain level of service, but costs less. Despite this, the Applicants continue to oppose DRA's recommendations.

The Applicants' first criticism of DRA's proposal is based on the false assumption that DRA is proposing a penalty only structure. The Applicants state that DRA's 'penalty-only' mechanism removes the financial incentives for the Applicants to attempt to improve service in customer service.[229] The Applicants' allegation is not true because DRA is not recommending a penalty-only structure

[227] Ex. DRA-24; p.24-4.

[228] Sempra Opening Brief, p.404: lines 22-24

[229] Sempra Opening Brief, p. 401; lines 19-22.

for the Applicants and has clearly indicated so in its testimony.[230] The Applicants recommend that the Commission reject DRA's proposal because "penalty-only mechanisms were rejected by the Commission in the Applicants' 2004 Cost of Service decision.[231]" Since the Applicants' premise is incorrect, this argument is irrelevant and should be rejected.

DRA recommends asymmetrical performance indicators that contain an equalization factor which equalizes rewards with penalties over the long run.[232] The Applicants argue that DRA is opposed to the symmetric reward/penalty structure because the Applicants have received more rewards than penalties. Excessive earning is not the cause, but the product, of incorrect system of performance incentives. DRA conducted a thorough analysis which identified that the Applicants receive more rewards than necessary for the benefit of ratepayers. DRA's rationale for asymmetrical performance indicators is based on the Commission's purpose for establishing performance indicators – to increase the quality of service in a manner that does not result in higher rates than necessary. The Commission stated this purpose when it first established Performance Incentives.[233]

The Applicants mischaracterize DRA's position by stating that DRA recommends a system where "the utilities are failing to meet half their Commission-adopted goals for customer service."[234] DRA makes no such recommendation. DRA recommends an approach where all penalties and rewards balance out in the long run, which, in turn, provides the maximum benefit for ratepayers. But DRA does not recommend such approach under the current

[230] Ex. DRA-39, p.39-4; lines 7-8.
[231] Sempra Opening Brief, p. 401; lines 22-24.
[232] Ex. DRA-39, p.39-4; lines 15-16.
[233] 68 CPUC 2d, 275.
[234] Sempra Opening Brief, p. 402: lines 20-23.

symmetric 50/50 penalty/reward structure. Certainly, if penalties and rewards balance out under the current 50/50 structure then, that would mean that utilities would be below benchmark as often as above benchmark. DRA alters the current symmetric structure to impose higher penalties than rewards so that, in the long run, the Applicants can earn an equal amount of dollars for penalties and rewards. Under DRA's system, the Applicants will have to improve in order to break even. Naturally, the Utilities attempt to characterize DRA's proposal as one that removes its incentive to improve.[235] DRA disagrees. If DRA's proposal is adopted and the Utilities have to follow these rules, then they will have plenty of incentive to improve.

Aglet has pointed out on page 38 of its Opening Brief that, on June 19, 2007, CityGroup Global markets issued a report citing Sempra Energy's "Continued ability to earn above the their cost of capital through incentive mechanisms." Aglet has further noted on page 39 of its Opening Brief that utility managers reprioritize resources in order to achieve incentive awards.[236]

Again, the Commission established performance incentive mechanisms to benefit ratepayers, not shareholders.[237] Any utility benefits and rewards derived from performance incentives are merely secondary results from the Commission's efforts to try to improve customer service for ratepayers. However, the symmetric rewards that have been in place for the companies from 1994 to 2006 have resulted in substantially more benefit to shareholders than ratepayers.[238]

DRA is proposing an incentive mechanism where the Applicants have enough incentives and penalties to improve, while maximizing ratepayer benefit at the same time. When designing service performance incentives, the Commission

[235] Sempra Opening Brief, p. 402: line 27.
[236] 5 RT 239:6-26, Reed,/SDG&E/the Applicants; 12 RT 1320:23, Fong,/SDG&E.
[237] 68 CPUC 2d, 275.
[238] Ex. DRA-39, p. 39-5:11-15.

should look at the end result, to maximize ratepayer customer service at the *lowest* price to them. DRA's asymmetric approach achieves that result. On the contrary, the Applicants want to set performance incentives in a way where they are the primary beneficiaries, which is contrary to the purpose of performance incentives.

28.1.2 Field Service Order Appointments (Applicable to both utilities)

DRA opposes the Applicants' proposal to change its Field Service Order Appointment indicator. The Applicants propose removing Appointments Met from the Appointments Provided and Met indicators.[239] Essentially, they want to obtain rewards based on the Appointments Provided. The actual service that is achieved for appointments is being able to timely meet the appointments, and not just schedule them. The only reason the Commission measures appointments provided is to compare it with the appointments actually met. Therefore, it does not make any sense to remove the main component of this indicator and provide rewards to the Applicants for scheduling appointments. Basically, the Applicants want to get rewards based on how many appointments they schedule, regardless if they ever meet these appointments, and ratepayers would have to pay 'rewards' for all the appointments the Applicants schedule, even if they do not meet any of them! If the Commission actually adopts the Applicants' recommendation, the Applicants will easily get a landslide of rewards for merely scheduling appointments. The Applicants' request is preposterous and should be rejected by the Commission. The Commission should not remove the only indicator that measures whether or not the Applicants meet their scheduled appointments.

The Applicants "believe that a double penalty attaches to the current structure,"[240] apparently because the Applicants also offer their customers a

[239] Ex. SCG-29, p.12.

[240] Sempra Opening Brief, p. 405: line 14-15.

$50.00 payment for a missed scheduled appointment.[241] The Applicants' argument is flawed because performance incentives measure the Applicants' appointments as a whole while the payment is directed at customer-specific appointments. The Applicants fail to take into account that incentives rewards and penalties and the $50.00 scheduling fee serve completely different purposes. The $50.00 missed appointment fee works to compensate individual ratepayers, a function not found in performance incentives. The Applicants can be rewarded for its good performance for field appointments, and yet at the same time, pay a few customers for missed appointments. The performance incentives and missed appointment payments are two entirely different regulatory functions. One measures and assesses penalties AND rewards at an institutional level and the other assesses only penalties at the individual customer level.

Furthermore, the Commission already addressed this issue in D.05-03-023. In that decision, the Commission upheld the current structure of the incentives which includes "Appointments provided" and "Appointments Met." The Commission stated:

> "for a customer who has had to miss work (often at an hourly wage) only to have the utility employee not appear within a reasonable window of time, the service guarantee is at least partial compensation and better than nothing. While the goal may be to improve overall service when individual customers are harmed, as with missed appointments, it is fully appropriate to have the compensation go to the individual.[242]"

The above passage leads to two conclusions. First, the service guarantee is merely "partial compensation." Therefore, the service guarantee cannot stand alone and should be accompanied by a service performance indicator. Second, the

[241] Ex. SCG-29, p.22.

[242] D.05-03-023, p.53.

Commission stresses the importance that the Applicants meet the appointments and do not harm the customer by not appearing within a reasonable window of time. Therefore, the Applicants should not eliminate "appointments met" as an indicator.

Clearly, in D.05-03-023, the Commission already addressed the service guarantee and concluded that it should exist together with the performance indicators. The Applicants have not provided a legitimate reason, or new facts, that warrant the Commission to alter its prior conclusion.

28.1.3 SDG&E Issues

SDG&E states that DRA's approach overstates the maximum rewards.[243] DRA's admits that SDG&E may not be able to realize the absolute maximum service rewards, but SDG&E exaggerates the extent it will have to improve in order to earn awards. For instance, with respect to Call Center responsiveness, SDG&E deduces that under DRA's proposal, it would be awarded $90,000 to achieve its personal best score of 87.1% calls answered within 60 seconds, and notes that this amounts to a 7.1% gain over SDG&E's proposed target of 80% calls answered within 60 seconds.[244] SDG&E goes on to state that "SDG&E cannot conceive of a reasonable circumstance where it would cost just an incremental $90,000 to have a 7.1% gain over SDG&E's proposed target of 80% calls answered within 60 seconds.[245]" In fact, SDG&E's present performance is 83.6% of calls answered within 60 seconds, based on the current three year average (from 2004 to 2006) and thus it needs only achieve a 3.5% gain to re-achieve its 87.1% personal best mark.[246]

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243 Sempra Opening Brief, p.409

244 Sempra Opening Brief, pp. 409-410.

245 *Id.*

246 Ex. DRA-24, pp. 24-29.

Clearly, DRA's asymmetric recommendation will reduce unnecessary bonuses for SDG&E and reduce ratepayer expenses, while maintaining the same or higher level of customer service. DRA does not expect SDG&E to welcome this approach because it will lose 'bonus' money. However, DRA continues to urge the Commission to adopt its asymmetric mechanism for the benefit of the ratepayers, and not the utilities.

28.1.3.1 Phone/Office Contact Satisfaction

SDG&E purposes that Office Satisfaction should be Monitor-Only.[247] SDG&E has not provided a justified reason as to why the Commission should remove this indicator. SDG&E states that because it closed three branches during 2005-2006, "neither the Commission nor SDG&E can know in advance the impact of these closures on office satisfaction."[248] Ironically, SCG provides the exact same rationale for removing Office Satisfaction as an indicator even though the situations differ, one relates to past closings and one relates to future closings. DRA is not convinced of either argument.

In order for the Commission to approve SDG&E's request, SDG&E has the burden to 1) prove that the office closures had an impact on performance incentives and 2) provide a compelling reason as to why that impact warrants excluding such an important indicator. SDG&E has not demonstrated how or provided evidence that the performance incentives will be impacted by the office closures. SDG&E merely states that the 2008 results are to be compared against a target that would be based on a forty office configuration.[249] SDG&E does not explain what impact this situation will have. SDG&E fails to meet its burden of proof, and the Commission should therefore reject its request.

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[247] Sempra Opening Brief, p. 410.
[248] Sempra Opening Brief, p. 410.
[249] Sempra Opening Brief, p. 405: lines 3-6.

28.1.4 SCG Issues

SCG equates DRA's agreement that SCG may not be able to reach its $1,500,000 maximum reward under DRA's equalization structure for Call Service Center Responsiveness to mean that "DRA's proposal is a penalty-only structure."[250] DRA also agreed that the practical maximum reward that SCG may receive would be $1,008,000 instead of $1,500,000. It appears that SCG has become too comfortable with receiving significant performance incentive awards because it views a reward of $1,008,000 versus $1,500,000 as a 'penalty.' Clearly, a problem exists when a company complains that in addition to its Rate of Return, its 'bonus' of $1,008,000 is a penalty.

Furthermore, such a scenario is highly unlikely to occur anyway. SGC admits that performance at 83% to 85% is feasible, meaning that it is unlikely that it can achieve its 100% maximum.[251] Clearly, DRA's asymmetric recommendation will reduce unnecessary bonuses for SCG and reduce ratepayer expenses, while maintaining the same or higher level of customer service. DRA does not expect SCG to welcome this approach because it will lose 'bonus' money. However, DRA continues to urge the Commission to adopt its asymmetric mechanism for the benefit of the ratepayers, and not the utilities.

28.1.4.1 Phone/Office Contact Satisfaction

DRA opposes SCG's proposal that the Office Satisfaction indicator be monitor-only, and the reward/penalty structure only be applied to Phone Satisfaction. SCG proposes to exclude rewards or penalties resulting for Office Satisfaction because it plans on closing seven of its forty-seven offices. SCG indicates that these seven office closures will somehow impact the office

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[250] Sempra Opening Brief, p. 403; lines 4-5 and lines 20-23.
[251] Sempra Opening Brief, p. 403.

satisfaction results because the target beginning in 2008 would be based on a survey that covered 47 offices.[252]

In order for the Commission to approve SCG's request, SCG has the burden to 1) prove that the office closures will have an impact on performance incentives and 2) provide a compelling reason as to why that impact warrants excluding such an important indicator. SCG has not demonstrated how or provided evidence that the performance incentives will be impacted by the office closures. SCG merely states that the 2008 results are to be compared against a target that would be based on a forty office configuration.[253] SCG does not explain what impact this situation will have. SCG fails to meet its burden of proof, and the Commission should therefore reject its request.

SCG and SDG&E requests are similar: that their Branch Office Satisfaction should be exempt from penalties/rewards. However, SDG&E's explanation is not that it is closing offices in the future, but that it closed offices in the past.[254] And similar to SCG, the company vaguely asserts that this impacts the performance incentives somehow and should be excluded. The companies have not provided sufficient reason for office satisfaction to be excluded as a working indicator.

Branch Satisfaction measures the customer service that SCG customers receive when they visit SCG's branch offices. SCG should be rewarded and penalized based on the service they give to customers who take the time and trouble to travel to reach the branch offices, therefore, the Commission should reject SCG's request from removing this very important indicator.

28.2 SDG&E Electric Reliability

SDG&E states that "SAIDI, SAIFI, and MAIFI have led to improved reliability for the majority of SDG&E customers and helped to direct reliability

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[252] Sempra Opening Brief, p. 404-405.
[253] Sempra Opening Brief, p. 405: lines 3-6.
[254] Sempra Opening Brief, p. 410.

investments and resources which have led to system wide improvements in reliability."[255] DRA agrees with SDG&E and recommends that these reliability indicators, with the exception of their asymmetric character, remain intact.

28.2.1 SAIDET

DRA opposes SDG&E's usage of SAIDET, a performance indicator previously unused by the Commission. SDG&E has not made a serious effort to calculate appropriate bench marks for it.[256] It is clearly premature to even consider adding a complicated new performance measure such as SAIDET, given the lack of historical data for this measure and SDG&E's lack of careful analysis of this measure. In fact SDG&E's arguments justifying its use of extrapolated SAIDET values rather than actual SAIDET values serve only to prove that SAIDET adds nothing new to the oversight mechanism[257]. SDG&E argues that its extrapolated SAIDET values are within 5% of the actual SAIDET values. However the extrapolated SAIDET values were a direct function of SAIDI values in the extrapolated years[258], raising the obvious question: why should a new indicator be added which can so accurately be evaluated using an already available indicator?

28.2.2 MAIFI

SDG&E states that SAIDI, SAIFI, and MAIFI are indices that are used throughout the industry[259], yet recommends that MAIFI be eliminated and that SAIDET be added.

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[255] Sempra Opening Brief, p. 418.
[256] Ex. DRA-24, p. 24-19; lines 19-23.
[257] Ex. SDG&E-209, page CAW-28, lines 9-20.
[258] Ex. DRA-24, p.24-20; lines 19-24.
[259] Sempra Opening Brief, p. 414.

SDG&E eliminates MAIFI from the reliability incentives. The Commission has used MAIFI for some time now and SDG&E has not provided any convincing reason as to why the Commission should depart from using MAIFI. Contrary to SDG&E's suggestion that MAIFI is not needed, MAIFI is an important indicator that tracks momentary electrical interruptions. It is essential that the Commission and utilities be able to track momentary electrical interruptions. Such momentary interruptions can cause users of computers to lose substantial data. The cost of momentary power interruptions to the U.S. economy has been estimated at $52.3 billion.[260]

Even SDG&E admits that MAIFI "has proven to be a useful performance indicator."[261] Yet, SDG&E argues that the Commission needs to eliminate MAIFI "because MAIFI will increase in the future."[262] MAIFI's increase in the future is the exact reason why it needs to be monitored if the Commission it to accomplish its purpose of achieving better service for ratepayers.

28.2.3 SAIFI

SDG&E opposes DRA's recommendation of 0.61 for SAIFI's target.[263] DRA's calculation is based on the current five-year average of 2002 to 2006 less a stretch factor of 0.01 outages, consistent with the Commission's decision on the 2004 Cost of Service proceeding. SDG&E supports DRA's usage of a five-year average, but states that DRA erred in calculating the target.[264] DRA 's calculation for SAIFI was based on SDG&E's response to CCUE Data Request DR-01, Question 9, Table CAW-6, excludes TMED and CPUC Major events. The phrase

[260] Ex. DRA-24, p. 24-18.
[261] Sempra Opening Brief, p. 456; line 12.
[262] Sempra Opening Brief, p. 456, lines 9-10.
[263] Sempra Opening Brief, p. 448.
[264] Sempra Opening Brief, p. 448; lines 14-21.

"excludes TMED" was left out of DRA's original testimony but was supplied as a correction on the stand.

28.2.4 The Commission Should Retain Deadbands

SDG&E argues that deadbands somehow provide reward or penalize for factors over which it has no control.[265] Deadbands are appropriate for reliability as they are for the other performance measures. In D.05-03-023 the Commission found that, "[i]t is clear that SDG&E's control over reliability is not perfect and is not total; we believe that deadbands protect against unwarranted rewards or penalties."[266]

The Commission has used deadbands for exactly the reason SDG&E gives for eliminating them in the case of reliability incentives – to prevent SDG&E from being rewarded based on factors beyond its control. In adopting deadbands, the Commission stated "because the targets are only a reasonable estimate – it is highly unlikely that SDG&E could directly influence the precise outcome and so it could see a penalty or reward as a matter of chance."[267] The Commission further stated that the inclusion of a deadband ensures that "minor random variances in performance do not trigger an undeserved penalty or reward." Deadbands protect consumers. The Commission should reject SDG&E's efforts to exclude the use of deadbands, as it has done in the past.

28.3 Employee Safety

Both SCG and SDG&E oppose DRA's asymmetric rewards/penalty structure for Employee Safety Incentives. The companies provide a list of unconvincing arguments, most of which have been addressed already.

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[265] Sempra Opening Brief, p. 446: lines 11-13.

[266] D.05-03-023, p.39.

[267] D.05-03-023, 2005 Cal. PUC LEXIS 127, *52 .

One argument against DRA's asymmetric rewards/penalty structure for Employee Safety Incentives that appears for the first time in the Opening Brief is the statement that "even DRA's own witness admits that he is not aware of the Commission ever employing such a concept."[268] The system of performance incentives is new and evolving, and the Commission is dealing with certain practices and procedures that it has not handled before – the novelty of a practice does not mean it is not a good idea.

In D.05-03-023, the Commission recognized that the rules and concepts needed to change by rejecting the Applicants' proposal of a 10-year status quo.[269] As D.05-03-023 suggests, the Commission should employ new methods and new rules to correct any defects present within the current structure of Performance Incentives. The Commission should disregard the Applicants' position that the Commission continue with the "status quo."

28.3.1 The Commission should reject the Settlement Agreement between SDG&E and CCUE

On October 10, 2007, SDG&E and the Coalition of California Utility Employees ("CCUE") filed a motion for adoption of a two-part settlement that would revise the terms of SDG&E's employee safety program. DRA urges the Commission to reject the Settlement Agreement because it is unreasonable. DRA concurs with Aglet that "CCUE and SDG&E offer no proof whatsoever that the settled incentives are necessary or cost effective."[270] Although DRA is opposed to the settlement, there is some merit to the settlement's reduction to the annual target which requires enhanced performance to earn a reward. However, the first

[268] Sempra Opening Brief, p. 465; line 8.

[269] D.05-03-023, p. 39. The Commission states "We do intend to adopt reasonable but challenging targets and not the 10-year status quo proposed by the applicant."

[270] Aglet Reply Brief, p. 13.

year target is too high, and it also provides too much reward opportunity for SDG&E which is contrary to DRA's asymmetrical proposal.

29. Monitoring, Reporting and Other Issues

DRA's recommendations for monitoring, reporting and other issues are addressed in Sections 7, 14, 27 and 28 of DRA's Opening Brief.

30. Conclusion

For all the foregoing reasons, and the reasons set forth in testimony, exhibits and in DRA's Opening Brief, DRA asks that its recommendations be adopted.

Respectfully submitted,

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November 5, 2007

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of **"REPLY BRIEF OF THE DIVISION OF RATEPAYER ADVOCATES"** in **Application 06-12-009, Application 06-12-010 and I.07-02-013** by using the following service:

[X] **E-MAIL SERVICE:** sending the entire document as an attachment to an e-mail message to all known parties of record to this proceeding who provided e-mail addresses.

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Executed in San Francisco, California, on the 5th day of November, 2007.

/s/ ANGELITA MARINDA

Angelita Marinda

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